COUNTY OF LOS ANGELES
DEPARTMENT OF AUDITOR-CONTROLLER

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AUDITOR-CONTROLLER

February 11, 2014

TO: Supervisor Don Knabe, Chairman
Supervisor Gloria Molina
Supervisor Mark Ridley-Thomas
Supervisor Zev Yaroslavsky
Supervisor Michael D. Antonovich

FROM: Wendy L. Watanabe
Auditor-Controller

SUBJECT: **OFFICE OF THE ASSESSOR – REVIEW OF PROPERTIES WITH A 20% OR GREATER REDUCTION IN VALUE (Board Agenda Item 36-A, April 10, 2012)**

At the April 10, 2012 meeting, your Board instructed the Auditor-Controller (A-C) to review four areas in the Office of the Assessor (Assessor), including a review of properties with a 20% or greater reduction in value (RIV) from January 2010 to May 2012 to determine appropriateness. We contracted with Rosenow Spevacek Group, Inc. (RSG) whom provides a variety of real estate consulting services to public agencies throughout the State of California, to perform the review. RSG subsequently obtained an independent appraiser, Lea Associates, who conducted the independent appraisals and the report is now complete.

Parameters of Review

The request for this review of properties with 20% or greater RIV followed public controversy regarding alleged favorable value reductions to property owners by the Assessor. As you know, the District Attorney (DA) initiated a criminal investigation on properties that may have been reduced inappropriately.

Sample Selection

From the Property Tax System, we determined that 149,115 (6.3%) of the 2.3 million properties within Los Angeles County had experienced a total RIV of 20% or greater between January 2010 and May 2012. These properties represented $35.2 billion

(3.26%) of the $1.08 trillion in the 2012 secured assessment roll. We focused on the property reductions that were initiated by the Assessor and sorted these properties by the 88 cities representing all supervisorial districts. Finally, we identified the top 20 parcels in each city with a RIV of 20% or more and judgmentally selected 117 of these properties for our review. The sample of 117 properties included 43 (37%) Single Family Residential properties, 28 (24%) Multi-Family Residential properties, and 46 (39%) Commercial/Industrial properties (see Exhibit I).

Summary of Findings

The A-C and RSG reviewed and analyzed 106 (90.5%) of the 117 properties and concluded with the following results:

Reasonable per A-C (37) and RSG Review (19); or Not Attributable to Market Decline (11): 67 (57.5%) of the 117 parcel reductions made by the Assessor were supportable either because the reductions appeared to be reasonable in our estimation or the RIV was not a result of market conditions but other factors including demolition, calamity, and roll corrections.

Inconclusive: 39 (33%) of the 117 parcel reductions made by the Assessor were deemed inconclusive, due to the unique land use and/or lack of comparable properties, the A-C and RSG could not make a determination on.

Warrant Further Analysis: 11 (9.5%) of the 117 properties were appraised by Lea Associates, with the following results:

Six (5%) of the 117 parcel reductions were relatively close to the appraised value as determined by Lea Associates.

Five (4.5%) of the 117 parcel reductions were lower than the appraisals prepared by Lea Associates. While appraisals can often yield varying opinions of value given the subjective nature of the field, using the County Assessor's procedures, the independent appraisal review by Lea Associates concluded that five parcels had Assessor's values that were significantly lower than the Lea Associates appraisal values. Of these five properties, all but one was reduced through Assessment Appeals Board (AAB) proceedings.

RIV Summary of 117 Properties

Results	# of Properties	% of Sample
Reasonable per A-C Review	37	32%
Reasonable per RSG Review	19	16%
Reasonable – Reductions Not Attributed to Market Decline	11	9.5%
Inconclusive (insufficient sales data)	39	33%
Warrant further analysis	11	9.5%
TOTAL	**117**	**100%**

Overall, for the 78 (117 – 39 Inconclusive) properties that a conclusion was reached, a difference of $30.8 million out of $382.8 million, or 8.06%, in assessed value was identified, as compared to the Assessor's assessed value of $413.6 million on the assessment roll (see Exhibit II).

Consultant's Review of Fraud

Throughout the review and analysis of the 117 properties, RSG found no indication of appraiser malfeasance. In addition, RSG was reluctant to conclude that any of the Assessor's valuations are erroneous, because in many cases, the contents of the parcel valuation files provided by the Assessor's office to the A-C as part of this review were not sufficiently detailed to understand how the Assessor's appraisers came to their assessed values.

RSG also indicated that the findings in this review should not be construed to reflect on assessments before or after the aforementioned 2-year period of review. The findings only pertain to the parcels analyzed, not the broader assessment roll, particularly since the properties were not randomly selected.

Consultant's Recommendations

After reviewing the Assessor's files and completing the appraisals, both RSG and Lea Associates concluded that the Assessor can improve in performing property appraisals. Specifically, consistent with A-C recommendations from prior Assessor audits, RSG suggests that the Assessor 1) needs to ensure that all property appraisals are properly documented in the property files; 2) appraisers conduct physical inspections on properties, particularly on high-end properties; and 3) should provide their appraisers with additional training to improve comparable property selection and knowledge of critical elements of comparison including clear height and lot coverage for industrial buildings, and avoiding out-of-market comparables. These recommendations are discussed in more detail in RSG's attached report.

Acknowledgement

We discussed the report with Assessor's management who, in all but two cases, conclude that the appraisals completed by their office are sound valuations. The Assessor has since corrected the values on the secured assessment roll; one has been increased and one has been decreased. Further, the Assessor agrees with one of the three recommendations and will implement accordingly and partially agree and disagree with the remaining two recommendations. The Assessor's response is attached, see Attachment II.

We thank Assessor management and staff for their cooperation and assistance throughout this review.

Please call me if you have any questions, or your staff may contact Susan Linschoten at (213) 974-8593.

WLW:SJL

Attachments

c: William T Fujioka, Chief Executive Officer
Sharon Moller, Chief Deputy Assessor
Sachi A. Hamai, Executive Officer, Board of Supervisors
Public Information Office
Audit Committee

Exhibit I

Department of Auditor-Controller
Office of the Assessor – Review of Properties with a 20% or Greater Reduction In Value (RIV)

Sample Selection Process	%	Parcel Count		Assessed Value	
Properties in Los Angeles County - 2012		**2,358,352**		**$ 1,079,700,000,000**	
Properties with a 20% or Greater RIV					
Single Family Residential	78%	116,542	6.3%	$ 16,546,269,775	3.26%
Residential Income	13%	19,903		$ 6,748,755,658	
Commercial/Industrial	9%	12,670		$ 11,925,011,423	
Total Properties with a 20% or Greater RIV	**100%**	**149,115**		**$ 35,220,036,856**	
Top 20 Property Reductions from each City with RIV of 20% or Greater		1,607			
Properties Selected for Further Analysis		**117**			

AUDITOR-CONTROLLER REVIEW

RIV – Reasonable

Single Family Residential	18
Residential Income	10
Commercial/Industrial	9
	37

32%

+

ROSENOW SPEVACEK GROUP (RSG) REVIEW

RIV – Reasonable

Single Family Residential	10
Residential Income	8
Commercial/Industrial	1
	19

16%

RIV – Not Attributed to Market (Calamity)

Single Family Residential	5
Residential Income	4
Commercial/Industrial	2
	11

9.5%

RIV – Inconclusive Insufficient Sales Data to Draw any Conclusion

Single Family Residential	8
Residential Income	5
Commercial/Industrial	26
	39

33%

+

LEA ASSOCIATES REVIEW

RIV – Warrants Further Analysis

Single Family Residential	2
Residential Income	1
Commercial/Industrial	8
	11

9.5%

=

TOTAL SAMPLE

Single Family Residential	43	37%
Residential Income	28	24%
Commercial/Industrial	46	39%
	117	**100%**

100%

Exhibit II

OFFICE OF THE ASSESSOR - REVIEW OF PROPERTIES WITH A 20% OR GREATER REDUCTION IN VALUE

Summary of 117 Sample Properties Reviewed and Analyzed

Parcel No.	Assessor Appraised Value	Appraised Value Analysis (1)	Variance in Assessed Value	Variance as % of Assessed Value
1	$ 217,589	$ 217,589	No Variance	0%
2	$ 4,993,692	$ 4,993,692	No Variance	0%
3	-	-	Inconclusive	-
4	$ 2,468,639	$ 2,468,639	No Variance	0%
5	$ 102,910	$ 102,910	No Variance	0%
6	$ 5,300,000	$ 7,000,000	$ (1,700,000)	-32%
7	-	-	Inconclusive	-
8	$ 2,193,000	$ 2,193,000	No Variance	0%
9	$ 430,000	$ 430,000	No Variance	0%
10	-	-	Inconclusive	-
11	$ 375,000	$ 375,000	No Variance	0%
12	-	-	Inconclusive	-
13	$ 262,000	$ 262,000	No Variance	0%
14	$ 273,000	$ 273,000	No Variance	0%
15	-	-	Inconclusive	-
16	$ 1,383,800	$ 1,383,800	No Variance	0%
17	$ 194,652	$ 194,652	No Variance	0%
18	$ 270,000	$ 270,000	No Variance	0%
19	$ 300,000	$ 300,000	No Variance	0%
20	-	-	Inconclusive	-
20	-	-	Inconclusive	-
21	$ 298,600	$ 298,600	No Variance	0%
22	$ 775,000	$ 1,050,000	$ (275,000)	-35%
23	-	-	Inconclusive	-
24	$ 161,542	$ 161,542	No Variance	0%
25	-	-	Inconclusive	-
26	$ 71,200,000	$ 71,200,000	No Variance	0%
27	$ 12,993,000	$ 12,993,000	No Variance	0%
28	$ 137,552	$ 137,552	No Variance	0%
29	-	-	Inconclusive	-
30	$ 314,608	$ 314,608	No Variance	0%
31	-	-	Inconclusive	-
32	$ 145,006	$ 145,006	No Variance	0%
33	$ 55,900,000	$ 69,000,000	$ (13,100,000)	-23%
34	$ 6,370,000	$ 6,370,000	No Variance	0%
35	$ 137,015	$ 137,015	No Variance	0%
36	-	-	Inconclusive	-
37	$ 1,021,245	$ 1,021,245	No Variance	0%
38	-	-	Inconclusive	-
39	$ 805,084	$ 805,084	No Variance	0%
40	$ 58,042	$ 58,042	No Variance	0%

(1) Appraised Value Analysis conducted by Auditor-Controller, Rosenow Spevacek Group (RSG), and Lea Associates

OFFICE OF THE ASSESSOR - REVIEW OF PROPERTIES WITH A 20% OR GREATER REDUCTION IN VALUE

Summary of 117 Sample Properties Reviewed and Analyzed

Parcel No.	Assessor Appraised Value	Appraised Value Analysis (1)	Variance in Assessed Value	Variance as % of Assessed Value
41	-	-	Inconclusive	-
42	$ 695,800	$ 695,800	No Variance	0%
43	-	-	Inconclusive	-
44	$ 254,919	$ 254,919	No Variance	0%
45	$ 840,000	$ 840,000	No Variance	0%
46	$ 1,336,000	$ 1,336,000	No Variance	0%
47	$ 900,000	$ 1,000,000	$ (100,000)	-11%
48	$ 225,000	$ 225,000	No Variance	0%
49	-	-	Inconclusive	-
50	$ 680,000	$ 680,000	No Variance	0%
51	-	-	Inconclusive	-
52	$ 7,000,000	$ 8,200,000	$ (1,200,000)	-17%
53	$ 1,600,000	$ 1,800,000	$ (200,000)	20%
54	$ 2,666,400	$ 2,475,000	$ 191,400	7%
55	$ 1,650,000	$ 1,650,000	No Variance	0%
56	-	-	Inconclusive	-
57	$ 802,700	$ 802,700	No Variance	0%
58	-	-	Inconclusive	-
59	-	-	Inconclusive	-
60	$ 406,000	$ 406,000	No Variance	0%
61	-	-	Inconclusive	-
62	$ 62,999	$ 62,999	No Variance	0%
63	-	-	Inconclusive	-
64	$ 634,000	$ 634,000	No Variance	0%
65	$ 594,000	$ 594,000	No Variance	0%
66	-	-	Inconclusive	-
67	$ 734,000	$ 734,000	No Variance	0%
68	$ 321,000	$ 321,000	No Variance	0%
69	$ 2,125,874	$ 2,125,874	No Variance	0%
70	-	-	Inconclusive	-
71	$ 390,372	$ 390,372	No Variance	0%
72	-	-	Inconclusive	-
73	$ 9,378,000	$ 9,700,000	$ (322,000)	-3%
73	$ 13,739,200	$ 13,000,000	$ 739,200	5%
74	-	-	Inconclusive	-
75	$ 13,760,000	$ 14,500,000	$ (740,000)	-5%
75	$ 10,400,000	$ 11,500,000	$ (1,100,000)	-45%
76	$ 3,800,000	$ 3,500,000	$ 300,000	8%
76	$ 3,100,000	$ 3,100,000	No Variance	0%
77	$ 348,000	$ 348,000	No Variance	0%
78	-	-	Inconclusive	-

(1) Appraised Value Analysis conducted by Auditor-Controller, Rosenow Spevacek Group (RSG), and Lea Associates

OFFICE OF THE ASSESSOR - REVIEW OF PROPERTIES WITH A 20% OR GREATER REDUCTION IN VALUE

Summary of 117 Sample Properties Reviewed and Analyzed

Parcel No.	Assessor Appraised Value	Appraised Value Analysis (1)	Variance in Assessed Value	Variance as % of Assessed Value
79	-	-	Inconclusive	-
80	$ 59,500,000	$ 71,000,000	$ (11,500,000)	-19%
81	-	-	Inconclusive	-
82	$ 735,193	$ 735,193	No Variance	0%
83	$ 60,000	$ 60,000	No Variance	0%
84	$ 698,600	$ 698,600	No Variance	0%
85	-	-	Inconclusive	-
86	$ 1,720,000	$ 1,720,000	No Variance	0%
87	$ 420,000	$ 420,000	No Variance	0%
88	$ 2,351,388	$ 2,351,388	No Variance	0%
89	$ 1,453,000	$ 1,453,000	No Variance	0%
90	-	-	Inconclusive	-
91	$ 747,000	$ 747,000	No Variance	0%
92	$ 1,252,000	$ 1,252,000	No Variance	0%
93	$ 3,273,000	$ 3,273,000	No Variance	0%
94	$ 2,876,000	$ 2,876,000	No Variance	0%
95	-	-	Inconclusive	-
96	$ 1,600,000	$ 1,600,000	No Variance	0%
97	$ 3,100,000	$ 3,100,000	No Variance	0%
98	-	-	Inconclusive	-
99	$ 1,649,000	$ 1,649,000	No Variance	0%
100	$ 24,000	$ 24,000	No Variance	0%
101	-	-	Inconclusive	-
102	$ 14,740,000	$ 14,740,000	No Variance	0%
103	$ 17,900,000	$ 17,900,000	No Variance	0%
104	-	-	Inconclusive	-
105	$ 1,248,000	$ 1,248,000	No Variance	0%
106	-	-	Inconclusive	-
107	$ 8,000,000	$ 8,000,000	No Variance	0%
108	-	-	Inconclusive	-
109	$ 3,850,000	$ 3,850,000	No Variance	0%
110	-	-	Inconclusive	-
111	$ 1,493,000	$ 1,493,000	No Variance	0%
112	$ 1,250,000	$ 1,250,000	No Variance	0%
113	-	-	Inconclusive	-
114	$ 1,880,000	$ 1,880,000	No Variance	0%
115	-	-	Inconclusive	-
116	$ 1,453,400	$ 1,453,400	No Variance	0%
117	$ 3,813,000	$ 3,813,000	No Variance	0%
Total	**$ 384,611,821**	**$ 413,618,221**	**$ (29,006,400)**	**-7.54%**

(1) Appraised Value Analysis conducted by Auditor-Controller, Rosenow Spevacek Group (RSG), and Lea Associates

RSG

BETTER COMMUNITIES. BOLDER FUTURES.

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Via Electronic Mail

Date: February 11, 2014

To: Wendy L. Watanabe, Auditor-Controller
COUNTY OF LOS ANGELES AUDITOR-CONTROLLER

From: Jim Simon, Principal
Jane Carlson, Senior Analyst
ROSENOW SPEVACEK GROUP INC.

SUBJECT: REVIEW OF LOS ANGELES COUNTY PROPERTIES WITH A 20% OR GREATER REDUCTION IN VALUE

EXECUTIVE SUMMARY

In April, 2012, the Los Angeles County Board of Supervisors requested that your office conduct a review of assessed value reductions of 20 percent or more to determine whether the reductions were warranted. The review followed public controversy reported at Board meetings and in local media regarding alleged favorable reductions in property values by Los Angeles County Assessor ("Assessor"). According to preliminary research by the County Auditor-Controller's office (ACO), between January 2010 and May 2012, 149,115 out of 2.3 million parcels in Los Angeles County experienced a total percentage change in value by 20 percent or more according to the County's Secured Tax Roll Database. The total 2012 assessed value of these 149,511 parcels represented 3.26% of the total 2012 assessed value of the 2.3 million parcels in Los Angeles County.

Under additional screening, 117 parcels were selected for further review by the ACO and Rosenow Spevacek Group, Inc. (RSG). Together, the ACO and RSG (along with RSG's independent appraiser subconsultant, Lea Associates) concluded as follows:

- Inconclusive: due to unique land use and/or lack of comparable properties, the ACO and RSG could not make a determination on 39 (33 percent) of the 117 parcel reductions in this review.

- Supportable Values: 67 (57.5 percent) of the 117 parcel reductions made by the Assessor were supportable either because the reductions appeared to be reasonable in our estimation or the reduction in value was not a result of market conditions but other factors including demolition, calamity, and roll corrections.

- The remaining 11 properties were appraised by Lea Associates, with the following results:

  - Values Reasonably Close: Six (5 percent) of the 117 parcel reductions were relatively close to the appraised value as determined by Lea Associates.

  - Values with a Difference in Opinion: Five (4.5 percent) of the 117 parcel reductions were lower than the appraisals prepared by Lea Associates. While appraisals can often yield varying opinions of value given the subjective nature of the field, using the County Assessor's procedures the independent appraisal review by Lea Associates concluded that 5 parcels had Assessor's values that were significantly lower than the Lea Associates appraisal values. Of these 5 properties, all but one was reduced through Assessment Appeals Board (AAB) proceedings.

  Together with the other six appraisals prepared by Lea Associates, the Assessor's values were collectively $30,848,400 lower than the opinion of Lea Associates.

In context of the 78 properties that this review reached a conclusion, the $30.8 million assessed value difference is approximately 8.06 percent of the total corresponding $382.8 million value of these properties. We stress that the findings in this analysis should not be construed to reflect on assessments before or after the aforementioned 2-year period of review. The findings only pertain to the parcels analyzed, not the broader assessment roll, particularly since the properties were not randomly selected. Further, throughout the review and analysis of the 117 properties, the ACO and RSG found no indication of appraiser malfeasance.

Despite the differences, RSG is reluctant to determine that the Assessor's valuations are erroneous, because in many cases, the contents of the parcel valuation files provided by the Assessor's office to the ACO as part of this review were not sufficiently detailed to understand how the Assessor's appraisers came to their values.

Four of the five parcels that had a material difference of value were reduced during the AABs process. RSG concurs that to better prepare Assessor staff for AAB proceedings, recommendations identified in the ACO's management audit of the Assessor's office dated January 3, 2013 should be implemented. Further, RSG understands that the Assessor's office has subsequently reviewed and modified practices, in part in response to other audit work performed by the ACO, which are expected to improve the accuracy of future assessments. If nothing else, improvements to the readiness and quality of documentation for property appraisals are properly included in the parcel files.

Lea Associates concluded that there are discrepancies between the Assessor's Real Property Handbook and standard appraisal practices as defined by the 2012-13 Uniform Standards of Professional Appraisal Practice (USPAP). Specifically, the Assessor's Real Property Handbook does not specifically require the use of verified sales, although Assessor practices and USPAP standards do require such verification of sales. This ambiguity in the Assessor's Real Property Handbook could result in a less rigorous analysis of comparable values by Assessor's staff. Also, Lea Associates recommends that physical inspection, particularly on high-end properties should be mandatory. Further, in reviewing the Assessor's files, Lea

Associates noted neglect of some of the crucial elements of valuation in selecting comparable properties, including age, type of construction, lot coverage, and out-of-market comparables.

RSG and Lea Associates recommend the following:

- **Consistent with ACO recommendation from prior Assessor audits, RSG agrees that Assessor's management needs to ensure that all property appraisals are properly documented in the parcel files.**

- **Assessor's management require appraisers to conduct physical inspections on properties, particularly on high-end properties.**

- **Assessor management should provide their appraisers with additional training to improve comparable property selection and knowledge of critical elements of comparison including clear height and lot coverage for industrial buildings, and avoiding out-of-market comparables, in order to enhance valuations.**

BACKGROUND

Role of the Los Angeles County Auditor Controller

Following allegations at Board meetings and in news media reports that some properties in the County were receiving favorable reductions in assessed value; the County Board of Supervisors requested in April 2012 that the ACO conduct a review of assessed value reductions of 20 percent or more over the past two years. Over that two year period, 149,511 out of 2.3 million parcels in Los Angeles County had a total percentage change in value of 20 percent or more. The total 2012 assessed value of these 149,511 parcels represented 3.26% of the total 2012 assessed value of the 2.3 million parcels in Los Angeles County.

The ACO was tasked with selecting declines for review and/or reappraisal representative of the alleged inappropriate declines that initiated the review. To arrive at a manageable sample size, the ACO selected the property reductions initiated by the Assessor's office on the Secured Tax Roll, and excluded parcels and declines from the 149,511 parcels, until they arrived at 14,151 parcels. Finally, the ACO sorted the 14,151 by city and judgmentally selected 117 parcels that represented the five supervisorial districts and most cities in the County to arrive at the best representative sample. One more parcel was added to the review because the Assessor had limited documentation to support a change in value due to a sale, and the available documentation suggested the property could have been undervalued by more than 20 percent. This sample of 117 parcels included 43 (37%) Single Family Residential properties, 28 (24%) Multi-Family Residential properties, and 46 (39%) Commercial/Industrial properties.

For the 117 parcels, the ACO reviewed all files located at the various Assessor district offices, including Major Properties. The ACO reviewed the parcel jackets, and followed-up with Assessor managers from each office when documentation was not found. Consequently, additional documents to support the declines were found in the Assessor's ADAPT System, their Shared Network Drive, and on the Appraisers' individual work computer, however, the Assessor staff could not find adequate support for all of the appraisals.

After the ACO's Secured Property Systems review, 37 parcels out of the 117 appeared to have reasonable declines in value and the ACO decided they needed no further review. The remaining 80 parcel files and accompanying Assessor documentation were isolated and transmitted to the ACO's property tax consultant, RSG, who identified additional properties that were reasonably reduced as well as other properties where there was a difference in value as explained below.

Role of Rosenow Spevacek Group, Inc

Because conducting appraisals on 80 properties would be extraordinarily time consuming, costly and potentially avoidable with some limited real estate analysis, RSG was tasked with identifying a small sample of the 80 parcel files they received, for possible appraisal or more-in-depth review. This work entailed two steps: 1) reviewing each parcel jacket assembled by the ACO to ascertain if adequate backup documentation was in place to support the Assessor's value, and 2) conducting an additional screening to determine if drops in values were inconsistent with surrounding properties of similar use.

The following is a summary of the review and screening process completed by RSG:

RSG's review of the parcel jackets proved to be inconclusive, as many of the property files lack notes and other supporting documentation to substantiate the work of the Assessor's appraisers and supervisorial staff. It was virtually impossible to conclude in any case whether the parcel jackets contained sufficient backup to justify the decisions by the Assessor, or even notes to explain how the AAB process affected some of the values. Details of the documentation issues, and the ACO's recommendations, are included in the Secured Property System audit of August 2013.

Next, RSG compared the 80 parcels in question to comparable property sales in each local market area to select properties that dropped by a larger percentage than surrounding properties. RSG staff members began the sales analysis by reviewing each file and identifying the lien date and final assessed value for each property after reassessment. If there were multiple years where the value declined, the year that saw the largest decrease in value was used and the accompanying ending assessed value. This information was all entered into a database.

The next step was to gather the comparable sales data. In order to isolate sales close to the Countywide lien date of January 1st, only sales that occurred from October 1st to March 31st (90 days before or after, consistent with Assessor's practices). Properties with a lien date of January 1, 2009 would only be compared to properties that sold between October 1, 2008 and March 31, 2009. Properties with a lien date of January 1, 2010 would only be compared to properties that sold between October 1, 2009 and March 31, 2010. And properties with a lien date of January 1, 2011 would only be compared to properties that sold between October 1, 2010 and March 31, 2011.

The analysis took into account not only the year in question, but land use characteristics and location. Different land uses can vary greatly in property value. So the properties in question were only compared to property sales for properties with the same land use. Values can also vary greatly across neighborhoods or districts. In order to account for geographic differences in property values throughout the County, sales comparables for the properties in question were further isolated by four different geographic levels, Countywide, 5 digit zip codes, 9 digit zip codes, and census tracts. That way a property in question could not only be compared to other properties that sold around the time the property was reassessed, but also to properties that sold within the same geographic area, possibly as close as the within the same census tract if sales data for that census tract during the specified time was available. This was not always the case and most properties were compared to sales within the entire County or their 5 digit zip code. While well-short of a detailed appraisal that would have superior accuracy, this approach was pursued because it was far more economical to evaluate 80 parcels in this manner versus immediately conducting appraisals.

Finally, RSG compiled all comparable sales by year, land use, and geographic area that could apply to each reassessed property in question and came up with a total number of sales, the average sales price, and the average sales price per square foot. These numbers were compared to the assessed value of the property in question and it's assessed value per square foot. Any assessed value or assessed value per square foot that was very different from the average sales price or price per square foot of comparable local properties was flagged for further review. If comparable sales data was not available, the property was marked as inconclusive.

The results of sales comparable screening fell into four basic categories:

1) 39 properties that had values that could not be confirmed by the sales comparable screening, typically due to their unique nature and/or limited number of comparable sales in the local area.
2) 19 properties had values that changed in a manner consistent with sales in the surrounding area and were not studied further. Still, one of these properties was included for further review by the ACO as part of their Secured Property Systems review. These 19 properties that had reasonable reductions are in addition to the initial 37 identified by the ACO.
3) 11 properties that were clearly reduced for reasons other than a decline-in-value, such as demolition, erroneous assessments, fire damage or other apparently appropriate reasons.
4) 11 properties assessed significantly lower (either by percentage or value) than peer properties in the local market area.

From this sales analysis, 11 parcels were flagged for appraisal. Therefore, of the 117 properties, 11 were flagged to be appraised by the independent appraiser, while RSG concluded that the values of the remaining 69 parcels were reasonable. A detailed breakdown of the above results is attached to this report.

The ACO also requested the AAB office provide the case files for those parcels (7 of the 11) that had a decline in value due to an AAB determination, and then forwarded the AAB documentation to RSG. This AAB information, in addition to the data from the Assessor's parcel jackets collected by the ACO, was provided to Lea Associates for reappraisal as described below.

<u>Role of Lea Associates (RSG Sub consultant/Independent Appraiser)</u>
Employing the County Assessor's Appraisal Manual as well as the standard practices of independent appraisers, Lea Associates conducted appraisals of the 11 flagged properties as a sub consultant to RSG. In some cases, more than one assessment year was in question, so Lea Associates prepared separate appraisal reports for each corresponding year in three instances.

Lea Associates identified 5 properties that appraised for significantly more than the Assessor's roll value. A summary of the results for those 5 properties is provided on the following pages.

It is important to note that this analysis was based on a 2 year period in time and that the findings should not be construed to reflect on assessments before or after that period in time. The findings below only pertain to the parcels analyzed, not the broader assessment roll.

RESULTS

In general, variances in appraisal opinions are not unusual, but significant variances were evident on 5 parcels evaluated by RSG and Lea Associates. Among the 11 parcels appraised by Lea Associates, there was a difference of $30.8 million of appraised property value for the properties, including 4 of which were reduced by several million dollars as part of the AAB hearing process. While Lea Associates appraisals are materially higher than the Assessors, we could not conclude after reviewing the limited information in the Assessor's files whether the Assessor's values are undervalued because records were frequently not sufficient to support the Assessor's final valuations. There may in fact be additional information available to the Assessor that was not provided to RSG (via the ACO) in this process that may support the Assessor's values, but it was not evident in the multi-phased effort to collect supporting documents employed by the ACO.

Details for the properties appraised are summarized below, presented in order of variance from the largest to smallest amount for each assessment. The complete Lea Associates appraisal report is contained under separate cover.

<u>Appraisal 1 (Commercial Office Building)</u>
Following adjustments during the assessment appeals process, this property was valued by the Assessor in 2010-11 at $55,900,000. Lea Associates utilized the Sales Comparison approach and the Income Capitalization Approach to determine their opinion of value, as of January 1, 2010 of $69,000,000. This is approximately 23 percent higher than the 2010-11 assessed value of $55,900,000.

Roll Year	Lien Date	% Decline	Region	Reason for Action	Assessed Value	Appraisal Opinion	Difference
2010-11	1/1/2010	37%	23	Prop 8 / AAB	$ 55,900,000	$ 69,000,000	$(13,100,000)

<u>Appraisal 2 (Commercial Office Building)</u>
Following adjustments during the assessment appeals process, this property was valued by the Assessor in 2009-10 at $59,000,000. Lea Associates utilized the Sales Comparison approach and the Income Capitalization Approach that yielded an opinion of value, as of January 1, 2009 of $71,000,000. This is approximately 20 percent higher than the 2009-10 assessed value of $59,000,000.

Roll Year	Lien Date	% Decline	Region	Reason for Action	Assessed Value	Appraisal Opinion	Difference
2009-10	1/1/2009	47%	23	Prop 8 / AAB	$ 59,500,000	$ 71,000,000	$(11,500,000)

<u>Appraisals 3A and 3B (Industrial Building)</u>
This property had two large declines in value in two different fiscal years. Both fiscal years and values were analyzed. After an assessment appeal was filed, the property was valued by the Assessor in 2009-10 at $13,760,000. Lea Associates utilized the Sales Comparison approach and the Income Capitalization Approach for both years to determine appropriate values for this property. Lea Associates' opinion of value, as of January 1, 2009 is $14,500,000. This is approximately 5 percent higher than the 2009-10 assessed value of $13,760,000.

The Assessor's office initiated a unilateral decline-in-value (also known by their former moniker "Proposition 8" reductions) adjustment in 2011-12 and dropped the assessed value down to $7,908,000. Comparatively, Lea Associates' opinion of value, as of January 1, 2011 is $11,500,000.

Roll Year	Lien Date	% Decline	Region	Reason for Action	Assessed Value	Appraisal Opinion	Difference
2009-10	1/1/2009	16%	27	AAB	$ 13,760,000	$ 14,500,000	$ (740,000)
2011-12	1/1/2011	36%	27	Prop 8	$ 7,908,000	$ 11,500,000	$ (3,592,000)

Appraisal 4 (Golf Course/Land)

Due to a successful assessment appeal, this property was valued by the Assessor in 2009-10 at $5,300,000. Lea Associates utilized the Sales Comparison approach and the Income Capitalization Approach to determine an appropriate value for this property. Based on this analysis, Lea Associates' opinion of value, as of January 1, 2009 is $7,000,000. This is approximately 32 percent higher than the 2009-10 value of $5,300,000

Roll Year	Lien Date	% Decline	Region	Reason for Action	Assessed Value	Appraisal Opinion	Difference
2009-10	1/1/2009	45%	28	Prop 8 / AAB	$ 5,300,000	$ 7,000,000	$ (1,700,000)

Appraisal 5 (Industrial Building)

Following a successful assessment appeal, this property was valued by the Assessor in 2010-11 at $7,000,000. Lea Associates; opinion of value, as of January 1, 2010 is $8,200,000. This is approximately 17 percent higher than the 2010-11 assessed value of $7,000,000.

Roll Year	Lien Date	% Decline	Region	Reason for Action	Assessed Value	Appraisal Opinion	Difference
2010-11	1/1/2010	37%	27	Prop 8 / AAB	$ 7,000,000	$ 8,200,000	$ (1,200,000)

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SHARON MOLLER
CHIEF DEPUTY ASSESSOR

February 11, 2014

TO: Wendy L. Watanabe
Auditor-Controller

FROM: Sharon Moller

SUBJECT: **RESPONSE TO REVIEW OF LOS ANGELES COUNTY PROPERTIES WITH A 20% OR GREATER REDUCTION IN VALUE**

We appreciate the efforts of you and your staff in conducting this review to determine the appropriateness of property reductions in excess of 20% between January 2010 and May 2012. We understand the difficulty of this assignment given the numerous and sometimes complex variables included in a property appraisal, and the level of appraiser judgment inherent in any final value conclusion. Despite differences in the judgments and opinions of value, it is important to note that RSG found no indication of appraiser malfeasance.

Concurrent to the review conducted by RSG, the Office of the Assessor was audited by the State Board of Equalization (BOE) for a portion of the period in question. In June 2013, the BOE released the *Los Angeles County Assessment Practices Survey* for the 2010-11 Assessment Roll. As a result of their sample appraisal study, we achieved an assessment accuracy ratio of 100.03 percent. In addition to the numerous procedural improvements made over the past year, the BOE audit findings confirm the adequacy of the standards and practices employed by our office and the accuracy of our appraisals.

In response to the Rosenow Spevacek Group Inc. (RSG) review dated December 17, 2013, the Office of the Assessor's Quality Assurance Section independently reviewed the 11 appraisals prepared by Lea Associates Property Economics. Our Quality Assurance Team members are highly-qualified, professional appraisers with advanced certification in property tax appraisal. After their independent analysis they identified areas of difference between the Assessor's valuations and the conclusions in the review completed by Lea Associates. In all but 2 cases, which we have since corrected (one assessed value increase and one decrease), we concluded that the appraisals completed by our department were sound valuations for property tax purposes based on the following observations:

- There is a judgment difference regarding the selection and adjustment of comparable sales. The Assessor's appraisals used sales more timely to the valuation date. The Lea Associates appraisals used "sales further back in time" and developed an "adjustment factor for changing market conditions." Given the unprecedented financial situation beginning in fall 2008, we question whether this adjustment factor adequately captures the significant, post-recession impact on property values.

- The Office of the Assessor is required to assess property at fair market value of the unencumbered fee simple interest. The independent appraisals prepared by Lea Associates include value conclusions based on the sales comparison approach with no indication that adjustments were made for existing leases that may be above or below market at the time of sale.

- In conformance with State Board of Equalization, Rule 4, and legal decisions, the Office of the Assessor is required to make allowances for differences between comparable properties and the subject. As further clarified in the State Board of Equalization AH 502, adjustments are required to be quantitative rather than qualitative. With the exception of the time adjustment, Lea Associates used qualitative adjustments. As specified in the AH 502, "While this may be a widely used and valid appraisal technique, it is not in accord with provisions of Rule 4." It should be noted that the Assessor's value conclusions typically fell within the range of value indicated by the sales comparison approach prepared by Lea Associates.

- In conformance with State Board of Equalization, Rule 8, "the capitalization rate is to include a property tax component, where applicable, equal to the estimated future tax rate." Rule 8 also specifies that property taxes are to be excluded from the calculation of net income. The methodology used by Lea Associates was to "load" the tax rate into the overall rate, then calculate and deduct the taxes from the expenses. While this methodology may result in a satisfactory conclusion, it is contrary to Rule 8 and may lead to instances of property taxes being accounted for twice (in the expense deduction and rate). It may also create inconsistency in the derivation and application of the appropriate capitalization rate. In accordance with Rule 8, the Assessor accounted for property taxes in the capitalization rate.

After careful consideration of market conditions and the collective evidence available to our Quality Assurance experts, we conclude that the estimates prepared by our staff fall within the range of market parameters and, with the exception of the 2 cases mentioned previously, reflect the full cash value of these properties in the midst of a rapidly declining real estate market. When we found that adjustments were warranted, we processed changes as indicated. In addition to our response to the three recommendations included in the Rosenow Spevacek Executive Summary, a more detailed analysis of the 5 properties with significantly different value conclusions is attached.

TT

Attachments

QUALITY ASSURANCE RESPONSE TO LEA ASSOCIATES ANALYSIS

According to the American Institute of Real Estate Appraisers, valuation is defined as "The process of estimating the market value, insurable value, investment value, or other properly defined value of an identified interest or interests in a specific parcel or parcels of real estate as of a given date."

In most cases, the Office of the Assessor is required to estimate the fair market value of the unencumbered fee simple interest (property title that is free and clear of any non-governmental encumbrances). These estimates are typically done for the lien date (January 1st) of any given year, or upon the occurrence of a reappraisable event such as a transfer or the completion of new construction. Most of the properties included in this sample were appraised on the lien dates for 2009 through 2011 in response to the market decline.

In most cases, fee appraisers, such as Lea Associates, estimate the fair market value of the leased fee interest (encumbered by a lease) of commercial properties that are encumbered for multiple years. The value of the fee simple interest can vary significantly from the leased fee interest, especially in a rapidly changing market. In many cases, a variation in value results from the legal requirement imposed on assessors to use current market rent rather than actual rent.

It is important to remember that during the time in question, there was a great deal of uncertainty concerning the real estate market and the economy at large. On July 9, 2009, Jon D. Greenlee, Associate Director, Division of Banking Supervision and Regulation, testified to the Board of Governors of the Federal Reserve System on the fragile state of the financial markets in the United States. His testimony addressed the gravity of commercial real estate markets with the lack of new issuance of commercial mortgage-backed securities since mid-2008, job losses, decline in property values, and higher underwriting standards (Exhibit 1A).

The most significant factor that separates our estimates from those developed by Lea Associates is the relative weight attributed to comparable sales that closed prior to the financial collapse. Lea Associates believes that physical similarity is more important than the timeliness of a sale. This may be true in a stabilized market; however, it is not advisable in a rapidly declining market caused by financial turmoil. According to the Appraisal Institute "Many appraisers make the tacit assumption that the local market is alive even when it is clearly dead or that an unmarketable property will somehow find a buyer. During the early 1990s and again in 2008 and 2009, most real estate markets showed a standoff between sellers unwilling to accept deep discounts and buyers unable to finance their purchases on acceptable terms. Older sales that reflected more favorable market conditions (or preceding an economic crisis) were deemed irrelevant" (Exhibit 1B).

The lack of market sales available after a financial crisis creates a significant challenge for any appraiser. Comparable sales are a critical element needed to support ones opinion of value; however, relying on sales that closed prior to the financial meltdown will likely result in conclusions that are not reflective of current market conditions. According to the CoStar Group "In fourth-quarter 2007, 180 closed transactions of Class A office sales of more than $5 million were recorded, trading at an average cap rate of 6.1% nationally. By the last three months of 2008, the average cap rate spiked to 7.6% on just 80 transactions, including a jump of more than 100 basis points between the third and fourth quarters. With sales results for the quarter still being collected, CoStar had recorded 42 closed transactions at an average actual cap rate of 7.9% as of March 18" (Exhibit 1C).

In addition to giving significant weight to untimely sales, Lea Associates' appraisals do not conform to the standards established by the State Board of Equalization (SBE). Property Tax Rule 4 sets forth the required elements in performing the Sales Comparison Approach to Value (Exhibit 2). Section (d) of Rule 4 states that the assessor shall:

"Make such allowances as he deems appropriate for differences between a comparable property at the time of sale and the subject property on the valuation date, in physical attributes of the properties, location of the properties, legally enforceable restrictions on the properties' use, and the income and amenities which the properties are expected to produce."

Rule 4 requires the assessor to make quantitative adjustments to comparable sales as opposed to qualitative adjustments. Assessor's Handbook AH 502 provides guidance from the State Board of Equalization on performing appraisals. AH 502 states, "Qualitative techniques compare comparable properties with the subject property by ranking them as 'superior' or 'inferior' (or similar terms) to the subject; adjustments not explicitly stated as either lump-sum dollar amounts or percentages. The subject property is then placed within the qualitatively ranked array of comparable sales in order to estimate its value. Appraisers often refer to this as 'bracketing' the subject property. While this may be a widely used and valid appraisal technique, it is not in accord with provisions of Rule 4" (Exhibit 3).
Court cases Mitchell v. County of Los Angeles and Main & Von Karman Associates v. County of Orange (Exhibits 4 and 5) further reiterate that quantitative adjustments need to be made as prescribed in Rule 4. Lea Associates did not make quantitative adjustments with the exception of time adjustments. As stated by the court, "Such an approach does not square with the spirit of Rule 4 which carefully lists specific adjustments that are to be made, nor with the reasoning of the State Board's general appraisal manual which states that, 'Each adjustment should receive separate and serious consideration.'"

Property Tax Rule 8 prescribes the standards that need to be foll owed in performing the Income Approach to Value (Exhibit 6). Section (c) states, "Property taxes, corporation net income taxes, and corporation franchise taxes measured by net income are also excluded from gross outgo." Section (f) states, "When the appraised value is to be used to arrive at an assessed value, the capitalization rate is to include a property tax component."

In performing the income approach for property tax purposes, the property taxes are accounted for in the capitalization rate, not the expenses. In several instances, Lea Associates included property taxes in their operating expenses. As stated above, this practice is not acceptable when valuing properties for tax purposes.

Our office conducted an analysis of the eleven properties reviewed, and identified several discrepancies between the departments' appraisals and those performed by Lea Associates. The summaries that follow provide clarification of the various assumptions and valuation procedures that led to significantly different value conclusions in the five instances noted in the Rosenow Spevacek Executive Summary:

1) [redacted] (Commercial Office Building)

The subject property is a large office building, 303,251 square feet. Lea Associates utilized the Sales Comparison approach; the sale dates of the comparable sales were from 2006 to 2008. There were minimal sales that occurred after the financial crisis started in the fall of 2008. Due to the lack of market sales data applicable to the valuation date, January 1, 2010, the Office of the Assessor did not apply the Sales Comparison approach. The subject property is an income producing property and in this case the Income Approach is the most applicable appraisal method to apply. Lea Associates' value indicated by the Income Approach is $66,150,000. The department's value is $55,900,000. The main difference between the estimates of value is the overall capitalization rate. Lea Associates' range of overall rates is from 5.0% to 9.04%. Three of the seven sales are small buildings, less than 10,000 square feet in size. Large office buildings would not attract the same type of investor/buyer as small office buildings. These investors would require different rates of return, lending and acquisition requirements, and capitalization rates. Of the four other sales, two of the sales had overall rates of 5.8% and 6.0% and sold in the first quarter of 2008, prior to the financial crisis. The two remaining sales sold in the second half of 2009, the overall rates are 9.0% and 9.04%. The market data that is most applicable to the valuation date supports a capitalization rate at the higher end of the spectrum. We selected an overall rate of 8.0%. Lea Associates utilized 7.0%.

2) [redacted] (Commercial Office Building)

The subject property is a large office building, 263,000$^+$ square feet. Due to the timing of the financial crisis and the same reasons discussed in #1, the most applicable and reliable methodology is the Income Approach for the valuation date of January 1, 2009. Lea Associates' value indicated by the Income Approach is $69,600,000. The assessed value is $59,500,000. The main difference between the estimates of value is the overall rate applied to the net income. Lea Associates' overall rate range is from 5.00% to 9.04%. They utilized the same six of the seven overall rate comparable sales in Property #1's appraisal. Three of the overall rate comparable sales are smaller buildings, less than 10,000 square feet in size. The remaining three are Lea Associates' most comparable overall rates which sold December 2009, September 2009 and March 2008 with overall rates of 9.0%, 9.04% and 5.80%, respectively. Again, a capitalization rate at the higher end of the spectrum is more appropriate considering the market conditions at that time. We selected an overall rate of 7.0%, and Lea Associates utilized 6.0%. In this case, a 1% variation in the overall rate results in a difference of approximately $10,000,000.

3A & B) [redacted] (Industrial Building)

The 2011 Prop 8 valuation was originally completed using the comparable sales approach arriving at an opinion of value of $7,908,000. Due to a clerical coding error, the appraiser was unaware that the subject property was a food processing plant containing cold storage as the property was coded incorrectly as a warehouse / distribution / storage facility. Since that time, the coding has been corrected and a new valuation has been performed using similar type comparable sales and income in the analysis. The corrected valuation indicated a fair market value of $10,400,000. Lea Associates opinion of value was $11,500,000 for January 1, 2011.

The January 1, 2009 valuations resulted in a 5% difference in the final opinions of value. The sales comparison approach performed by the Office of the Assessor resulted in a price per square foot of

$158. The range of comparable sales used by Lea Associates produced a price per square foot range of $97 to $183. Quantitative adjustments were made by the Office to the comparable sales to account for characteristic differences between the subject and comparable sales. Lea Associates did not make quantitative adjustments.

4) [redacted] (Golf Course / Land)

The primary difference in the opinions of value between Lea Associates and the Office of the Assessor resulted from the method used to estimate the potential net operating income. The Office utilized the actual operating income and expense statements supplied by the golf course facility. Lea Associates only had access to market surveys which can vary significantly. Based on the actual data which reflected the decline in golf rounds and green fees as the economy worsened, the Office of the Assessor established a baseline and then projected a gradual increase of income over the next three years from the January 1, 2009 valuation date. The Office relied on a discounted cash flow model, while Lea Associates applied a direct capitalization of what they perceived to be stabilized anticipated income and expenses.

Golf is a recreational sport that is sensitive to variations in expendable income which significantly declined following stock market losses in the fall of 2008. Based on actual income, the Office anticipated green fees of $190 per round for year 2009 and escalated them to $200 by year 2011. Lea Associates relied on a survey of green fees collected during 2007 and 2005 which indicated a range of $78 to $250 per round and estimated a stabilized rate of $200 for 2009.

Other differences included allowable operating expenses. It appears that Lea Associates included property tax and ground lease fees in their expense ratio which, by Property Tax Rule 8, are to be excluded from valuations intended for property tax purposes. It also appears that the tax rate was included in Lea Associates capitalization rate which indicates that the property tax was accounted for twice. In addition, we were unable to determine if Lea Associates accounted for the actual cost of goods sold due to insufficient documentation.

5) [redacted] (Industrial Building)

The original January 1, 2010 valuation prepared by the Office indicated an opinion of value of $8,100,000, which is within 1.2% of Lea Associates' opinion of value of $8,200,000. The appraisal was prepared as a recommendation for reduction for a pending assessment appeal case. The recommendation was modified on the day of the hearing to $7,000,000 as a response to new income and sales comparable information presented by the taxpayer's agent. The new information provided additional capitalization rate comparable sales indicating a range of 8.0% to 10.4%. Lea Associates used 6.5% in their analysis and the Office used 7%. The agent, Lea Associates, and the Office of the Assessor all shared similar rent income but the agent indicated a higher vacancy factor for the subject and higher operating expenses than used by both Lea Associates and the Office of the Assessor. The agent's indicated opinion of value was $5,550,000, but the Assessor's Representative felt that $7,000,000 was reasonable based on newly presented data including three additional comparable sales ranging from $82.95 to $96.60 per square foot.

Response to Recommendations – Review of Los Angeles County Properties With a 20% or Greater Reduction in Value

1. **Assessor's management ensure that all property appraisals are properly documented in the parcel files.**

Department Response: **AGREE**

As stated in the Review of the Office of the Assessor's Secured Property Tax System Audit response, dated June 7, 2013, (attached), although it is standard appraisal practice to consider all sources of information (including information provided by the property owner) and exercise appraiser experience and judgment in determining a value conclusion, the Office recognizes that these judgments may not be sufficiently noted in certain appraisals. Assessment Services/Appraisal Standards will create policies and procedures for sufficient documentation of the various types of property appraisals. This shall include guidelines of noting where supplementary information that is considered but not contained in a valuation is located. Real property appraisal staff will be required to adhere to these requirements which will also be added to our training program. Periodic quality assurance reviews will be conducted following implementation in order to ensure compliance. Additionally, the following system changes shall be made to enhance the documentation of and justification for value conclusions:

- Both PTS and DIV systems shall prohibit an appraisal to be submitted without a comment when an appraiser selects a value to enroll other than the calculated appraised value.
- Both PTS and DIV systems shall prohibit a value conclusion to be submitted without a comment if it is submitted with the "Enroll Other" value option.

2. **Assessor's management require appraisers to conduct physical inspection of properties, particularly on high-end properties.**

Department Response: **DISAGREE**. A physical inspection is not required for all properties.

In their executive summary, RSG states, "Lea Associates concluded that there are discrepancies between the Assessor's Real Property Handbook and standard appraisal practices as defined by the 2012-13 Uniform Standards of Professional Appraisal Practice (USPAP)." They go on to say that the Assessor's Office "makes optional the physical inspection of the subject property" and recommends that "physical inspection, particularly on high-end properties should be mandatory."

California Assessors are governed by the Revenue and Taxation Code and the State Board of Equalization, not USPAP. Furthermore, USPAP does not require inspection of subject properties, but does require appraisers governed by these standards to disclose whether or not they personally conducted one.

According to Advisory Opinion 2, published by the Appraisal Standards Board (ASB), "An inspection is not required by USPAP, but one is often conducted." Also included in this publication is the explanation that "The extent of the inspection process is an aspect of the scope of the work, and may vary based on assignment conditions and the intended use of the assignment results. It is the appraiser's responsibility to determine the appropriate scope of work, including the degree of inspection necessary to produce credible assignment results given the intended use."

In most cases, it is highly advisable to conduct an inspection of the subject property being appraised for an assessment appeal, especially when it is high-end or complex. However, it is not practicable or cost effective to mandate inspection in each and every case. Similar to the USPAP guidelines, we rely on our staff to evaluate the specific challenges associated with any given assignment and determine whether or not an inspection is necessary to produce an appraisal that is appropriate for its intended use.

3. **Assessor management provide additional training of appraisers and supervisors to enhance valuations by selecting comparable properties, including age, type of construction, lot coverage, and out-of-market comparables.**

Department Response: **PARTIALLY AGREE**

The Office is in compliance with this recommendation. As stated in the One-Year Report on Assessor Operations dated July 18, 2013, the Office of the Assessor sponsored a training program on residential-income properties (apartments) presented by the Appraisal Institute. This advanced appraisal course on residential-income valuation for some of the appraisal staff was completed in April 2013. For those appraisers that were not selected to attend the training program presented by the Appraisal Institute, the Assessor's Training Section created a 4-hour truncated version of that training and approximately 150 appraisers attended. The Appraisal Institute will return the last week in September and the beginning of October 2013 to provide advanced training on t he Income Approach to 70 appraisers. Appraisal staff also attended various seminars sponsored by the International Association of Assessing Officers (IAAO) on numerous topics. Additional Appraisal Institute courses are under review by the Assessor's Training Section and will be implemented as funds allow. All in addition to the one-year training program that all appraisers are required to complete to gain certification through the State Board of Equalization, and the 24 hours of Board of Equalization Mandated In-Service-Training provided annually to maintain that certification.

The training that is provided to the appraisal staff clearly covers the "crucial elements of valuation in selecting comparables." The determination of which elements of comparison are more important to consider in the selection and adjustment process is part of the appraisal process. Although proximity and physical characteristics are certainly important considerations, the timeliness of the comparable sale is essential, particularly in an annual decline-in-value appraisal. According to the Appraisal Institute, "During the early 1990s and again in 2008 and 2009, most real estate markets showed a standoff between sellers unwilling to accept deep discounts and buyers unable to finance their purchases on acceptable terms. Older sales that reflected more favorable market conditions (or preceding an economic crisis) were deemed irrelevant." Our appraisers would face a difficult, if not unsupportable, defense of their post-recession, 2010 valuations if they used comparables from sales dating as far back as 2005. Therefore, we respectfully disagree with the conclusion that the comparables selected by the Assessor were the result of a "neglect of some of the crucial elements of valuation." To the contrary, they were considered more supportable indications of market value for the valuation dates given the extraordinary, post-recession condition of the market at that time.

We continue to support additional training for our professional staff. We have supplemented our training with additional reference tools such industry periodicals and publications, as well as access to data sources such as CoStar, RealQuest, and the Multiple Listing Service. As stated in the Department's Strategic Plan dated March 2013, additional licenses of the Multiple Listing Service, a tool vital to the work of appraisers, were obtained to increase the accuracy of appraisals and reduce the number of assessment appeals cases in the future.

Exhibit 1A

Jon D. Greenlee

Testimony

Board of Governors of the Federal Reserve System

Testimony

Jon D. Greenlee, Associate Director, Division of Banking Supervision and Regulation

Commercial real estate

Before the Joint Economic Committee, U.S. Congress, Washington, D.C.
July 9, 2009

Chair Maloney, Vice Chairman Schumer, Ranking Members Brownback and Brady, and other members of the Committee, I am pleased to be here today to discuss several issues related to commercial real estate (CRE) lending in the United States. I will start by describing the current conditions in CRE markets, then discuss Federal Reserve efforts to help revitalize CRE markets and promote lending to creditworthy borrowers. I will also outline Federal Reserve supervisory actions relating to CRE, and discuss the need to ensure a healthy balance between strong underwriting, risk management, and financial institution safety and soundness on the one hand, and credit availability, on the other.

Current Conditions in CRE and CMBS Markets

Financial market dislocations and the continuing economic downturn are clearly challenging CRE markets. The pace of property sales has slowed dramatically since peaking in 2007, from quarterly sales of roughly $195 billion to about $20 billion in the first quarter of 2009. Demand for commercial property is sensitive to trends in the labor market, and, as job losses have accelerated, tenant demand for space has declined and vacancy rates have increased.

The decline in the CRE market has been aggravated by two additional factors. First, the values of commercial real estate increased significantly between 2005 and 2007, driven by many of the same factors behind the residential housing bubble, resulting in many properties either purchased or refinanced at inflated values. Prices have declined about 24 percent since their peak in the fall of 2007 and market participants expect significant further declines. Second, the market for securitized commercial mortgages (CMBS), which accounts for roughly one-fourth of outstanding commercial mortgages, has been largely dormant since early 2008 while many banks have substantially tightened credit. The decline in property values and higher underwriting standards in place at banks will increase the potential that borrowers will find it difficult to refinance their maturing outstanding debt, which often includes substantial balloon payments.

The higher vacancy levels and significant decline in value of existing properties has also placed pressure on new construction projects. As a result, the construction market has experienced sharp declines in both the demand for and the supply of new construction loans since peaking in 2007.

The negative fundamentals in the commercial real estate property markets have broadly affected the credit performance of loans in banks' portfolios and loans in commercial mortgage backed securities. At the end of the first quarter of 2009, there was approximately $3.5 trillion of outstanding debt associated with commercial real estate. Of this, $1.8 trillion was held on the books of banks, and an additional $900 billion represented collateral for CMBS. At the end of the first quarter, about seven percent of commercial real estate loans on banks' books were considered delinquent.[1] This was almost double from the level a year earlier. The loan performance problems were the most striking for construction and land development loans, especially for those that finance residential development. Notably, a high proportion of small and medium-sized institutions continue to have sizable exposure to commercial real estate, including land development and construction loans, built up earlier this decade, with some having concentrations equal to several multiples of their capital.

The Federal Reserve's Senior Loan Officer Opinion Survey regularly provides useful information about lending conditions. In the most recent survey, conducted in April of this year, almost two-thirds of the domestic banks surveyed reported having tightened standards and terms on commercial real estate loans over the previous three months. Additionally, almost two-thirds of the respondents reported weaker demand for CRE loans, the highest net percentage so reporting since the survey began tracking demand for CRE loans in April 1995.

The current fundamentals in CRE markets are exacerbated by a lack of demand for CMBS, previously a financing vehicle for about 30 percent of originations. New CMBS issuance has come to a halt as risk spreads widened to prohibitively high levels in response to the increase in CRE specific risk and the general lack of liquidity in structured debt markets. There has been virtually no new issuance since the middle of 2008. Increases in credit risk have significantly softened demand in the secondary trading markets for all but the most highly rated tranches of these securities. Delinquencies of mortgages in CMBS have increased markedly in recent months and market participants anticipate these rates will climb higher by the end of this year, driven not only by negative fundamentals but also borrowers' difficulty in rolling-over maturing debt. In addition, the decline in CMBS prices has generated significant stresses on the balance sheets of institutions that must mark these securities to market.

Federal Reserve Activities to Help Revitalize CRE Markets

U.S. government agencies have taken a number of actions to strengthen the financial sector and to promote the availability of credit to businesses and households. In addition to aggressive actions related to monetary policy, the Federal Reserve has taken strong actions to improve liquidity in financial markets by establishing numerous liquidity facilities. One of the more recent liquidity programs is the Term Asset-Backed Securities Loan Facility (TALF), begun in November 2008, to facilitate the extension of credit to households and small businesses.

In an effort to target CMBS markets, in May of this year, the Federal Reserve announced that, starting in June 2009, certain newly issued high quality CMBS would become eligible collateral under the TALF, followed in July by high quality "legacy" CMBS issued before January 1, 2009. The provision of TALF financing for newly issued CMBS was intended to support new lending for creditworthy properties, especially those whose loans are set to mature soon. TALF financing for legacy CMBS was intended to lower secondary market spreads and enhance liquidity. Lower spreads should then encourage new lending and ease the balance sheet pressures on owners of CMBS. The resulting improvement in CMBS markets should facilitate the issuance of new CMBS, thereby helping borrowers finance new purchases of commercial properties or refinance existing commercial mortgages on better terms.

TALF loans will be offered to finance new issuances of CMBS and purchases of legacy CMBS once a month. No TALF loans collateralized by new CMBS have been made yet, in part because CMBS take some time to arrange. The first subscription to include legacy CMBS will be on July 16, 2009.

Federal Reserve Supervisory Activities Related to CRE

The Federal Reserve has been focused on commercial real estate (CRE) exposures at supervised institutions for some time. As part of our supervision of banking organizations in the early 2000s, we began to observe rising CRE concentrations. Given the central role that CRE lending played in the banking problems of the late 1980s and early 1990s, we led an interagency effort to issue supervisory guidance on CRE concentrations in 2006. In that guidance, we emphasized our concern that some institutions' strategic- and capital-planning processes did not adequately acknowledge the risks from their CRE concentrations. We stated that stress testing and similar exercises were necessary for institutions to identify the impact of potential CRE shocks on earnings and capital, especially the impact from credit concentrations.

As weaker housing markets and deteriorating economic conditions have impaired the quality of CRE loans at supervised banking organizations, we have devoted significantly more supervisory resources to assessing the quality of regulated institutions' CRE portfolios. These efforts include monitoring carefully the impact that declining collateral values may have on institutions' CRE exposures as well as assessing the extent to which banks have been complying with the interagency CRE guidance. Reserve Banks with geographic areas suffering more acute price declines in real estate have been particularly focused on evaluating exposures arising from CRE lending. We have found, through horizontal reviews and other examination activities, that many institutions would benefit from additional and better stress testing, improved management information systems, and stronger appraisal practices, and that some banks need to improve their understanding of how concentrations–both single-name and sectoral/geographical concentrations--can impact capital levels during shocks.

The recently concluded Supervisory Capital Assessment Process (SCAP) provides a perspective of the risks of CRE exposures. The 19 firms reviewed in the SCAP had over $600 billion in CRE loans, of which more than half were for nonfarm / non residential properties, and about one-third were related to construction and land development. The SCAP estimated that cumulative two-year CRE losses under the adverse scenario, in which residential house prices would continue to fall dramatically in 2009 and 2010, would be more than eight percent of total CRE exposures, with losses on construction loans significantly higher. Using information gained from the SCAP simulation exercise, we are also working with smaller firms that have substantial CRE exposures to ensure that their risk management practices are adequate and that they continue to maintain appropriate reserves and capital to support an expected increase in CRE losses.

As part of our ongoing supervisory efforts related to CRE, we implemented additional examiner training so that our examiners are equipped to deal with more serious CRE problems at both community and regional banking organizations on a consistent basis. Further, we have enhanced our outreach to key real estate market participants and obtained additional market data sources to help support our supervisory monitoring activities. We have also issued guidance to our examiners on real estate appraisals, proper use of interest reserves in construction and development loans, evaluation of loan loss reserving methodologies, and troubled debt restructuring practices.

Maintaining Balance in the Supervisory Process
The Federal Reserve has long-standing policies and procedures in place to promote institutions' risk identification and management practices that support sound bank lending and the credit intermediation process. In fact, guidance issued in 1991, during the last commercial real estate crisis, specifically instructs examiners to ensure that regulatory policies and actions do not inadvertently curtail the availability of credit to sound borrowers.[2] The 1991 guidance also states that examiners are to ensure that supervisory personnel are reviewing loans in a consistent, prudent, and balanced fashion.

The 1991 guidance covers a wide range of specific topics, including the general principles that examiners follow in reviewing commercial real estate loan portfolios, the indicators of troubled real estate markets, projects, and related indebtedness, and the factors that examiners consider in their review of individual loans, including the use of appraisals and the determination of collateral value. Credit classification guidelines were also addressed.

This emphasis on achieving an appropriate balance between credit availability and safety and soundness continues, and applies equally to today's CRE markets. Consistent with the 2006 CRE guidance, institutions that have experienced losses, hold less capital, and are operating in a more risk-sensitive environment are expected to employ appropriate risk-management practices to ensure their viability. At the same time, it is important that supervisors remain balanced and not place unreasonable or artificial constraints on lenders that could hamper credit availability.

As part of our effort to help stimulate appropriate bank lending, the Federal Reserve and the other federal banking agencies issued regulatory guidance in November 2008 to encourage banks to meet the needs of creditworthy borrowers.[3] The guidance was issued to encourage bank lending in a manner consistent with safety and soundness--specifically, by taking a balanced approach in assessing borrowers' ability to repay and making realistic assessments of collateral valuations.

More generally, we have directed our examiners to be mindful of the pro-cyclical effects of excessive credit tightening. Across the Federal Reserve System, we have implemented training and outreach to underscore these intentions. We are mindful of the potential for bankers to overshoot in their attempt to rectify lending standards, and want them to understand that it is in their own interest to continue making loans to creditworthy borrowers.

Conclusion
Financial markets in the United States continue to be somewhat fragile, with CRE markets particularly so.

Banking institutions have been adversely impacted by recent problems in CRE markets. The Federal Reserve, working with the other banking agencies has acted--and will continue to act--to ensure that the banking system remains safe and sound and is able to meet the credit needs of our economy. We have aggressively pursued monetary policy actions and provided liquidity to help repair the financial system. The recent launch of the CMBS portion of the TALF is an effort to revitalize lending in broader CRE markets. In our supervisory efforts, we are mindful of the risk-management deficiencies at banking institutions revealed by the current crisis and are ensuring that institutions develop appropriate corrective actions. Within the Federal Reserve, we have been able to apply our interdisciplinary approach to addressing problems with CRE markets, relying on supervisors, economists, accountants, quantitative analysts, and other experts.

It will take some time for the banking industry to work through this current set of challenges and for the financial markets to fully recover. In this environment, the economy will need a strong and stable financial system that can make credit available. We want banks to deploy capital and liquidity, but in a responsible way that avoids past mistakes and does not create new ones. The Federal Reserve is committed to working with other banking agencies and the Congress to promote the concurrent goals of fostering credit availability and a safe and sound banking system.

Footnotes

1. Loans 30 or more days past due. Return to text

2. "Interagency Policy Statement on the Review and Classification of Commercial Real Estate Loans," (November 1991). Return to text

3. "Interagency Statement on Meeting the Needs of Credit Worthy Borrowers," (November 2008). Return to text

Return to top

2009 Testimony
Last update: July 9, 2009

Exhibit 1B

The Appraisal Institute:

Appraising the Appraisal

Appraisal Institute®
Professionals Providing Real Estate Solutions

Appraising the Appraisal

The Art of Appraisal Review

Second Edition

by Richard C. Sorenson, MAI

Appraisal Institute • 550 West Van Buren • Chicago, IL 60607 • www.appraisalinstitute.org

The Appraisal Institute advances global standards, methodologies, and practices through the professional development of property economics worldwide.

use does not meet the basic definition of a comparable sale–i.e., a property that the market would view as being competitive with the subject. No adjustment or narrative explanation can reconcile two properties that have different highest and best uses. Use of this type of incompatible property in the comparative analysis is a red flag in a report.

Use of properties that have dramatically different tenancy profiles as comparables. Consider the use of a multitenant, 100,000-sq.-ft. warehouse as a comparable property in the appraisal of a single-tenant, 100,000-sq.-ft. warehouse. A sophisticated client would likely ask why the typical purchaser of the single-tenant warehouse would be interested in buying the multitenant property being used as the comparable. Similarly, properties of different sizes appeal to different buyer-seller profiles, so 20,000- to 40,000-sq.-ft. industrial buildings are not comparable to a 150,000-sq.-ft. facility.

Merely stating the sale prices of comparable properties with no additional facts or analysis. The date of sale, the grantor, the grantee, the transaction sale price, the cash-equivalent sale price, the terms of sale, the conditions of sale, the units of comparison, and the occupancy at the time of sale are all critical to the appraiser's analysis and the client's understanding of that process. Depending on the scope of work of the review assignment, the reviewer may need to confirm much of this data.

Not recognizing the availability or lack of willing sellers and actual buyers with access to funds. Many appraisers make the tacit assumption that the local market is alive even when it is clearly dead or that an unmarketable property will somehow find a buyer. During the early 1990s and again in 2008 and 2009, most real estate markets showed a standoff between sellers unwilling to accept deep discounts and buyers unable to finance their purchases on acceptable terms. Older sales that reflected more favorable market conditions (or preceding an economic crisis) were deemed irrelevant.

Lumping value-influencing differences together. When quantitative adjustments are made in a comparative analysis, they should not be aggregated. Doing so prevents the reviewer or user of the report from checking the comparative analysis for consistency or contradiction, thus rendering all the adjustments suspect. A major error reviewers often encounter is the lumping together of several inequalities into a single dollar or percentage adjustment. When inequalities are considered offsetting, they should not be lumped together in a manner that hides the relative importance of each item. The reviewer must be able to assess the relative significance of each difference that influences value in the market.

Exhibit 1C

CoStar Group
Survival Mode

CoStar GROUP
Real Estate Information

News: National

March 18, 2009
Written by Randyl Drummer (rdrummer@costar.com)

SURVIVAL MODE: Rising Cap Rates Add to Real Estate Investors' Worries

With Tenants in the Driver's Seat, Landlord Find Themselves In Survival Mode As Property Values Fall and Revenue Shrinks

The steady rise in capitalization rates from the sale of commercial property shows little sign of abating, adding to the anxiety of real estate investors who don't expect any of the major property sectors to rebound until well into next year.

When cap rates rise, asset values fall, and as investment risk has increased, actual cap rates have risen nationally over the last five quarters -- and continue to rise across most markets and property types, according to a preview analysis of CoStar COMPs data gathered so far in 2009. The continued cap rate expansion also dovetails with the results of the first-quarter Korpacz Real Estate Investor Survey, a widely watched report issued by PricewaterhouseCoopers this week.

More than 100 institutional and private investors surveyed for the Korpacz report predicted that cap rates will rise by an average of nearly 50 basis points over the next six months across virtually all property categories and most metro markets. The largest projected gainers are power centers (74.4 bp) suburban office (65.6 bp) and regional malls (65 bp), with their generally lower barriers to market entry. Although cap rates appear to have dropped in the Houston and Washington, D.C. office markets in the first quarter, Korpacz respondents expect them to rise a whopping 118 points and 25 points, respectively, over the next six months.

"The ongoing problems tied to both the U.S. economic recession and the financial crisis are making it very difficult for investors to sidestep value losses across all property types," said Susan Smith, director in the PricewaterhouseCoopers real estate sector services group and editor of the survey. "It's clear that many investors are more in survival mode than in acquisition mode, even though buying opportunities are expected to increase in the coming months."

The 100-page survey provides a window into the thought processes of the investors in REITs, pension funds, private equity firms and insurance and mortgage companies on the economy, property valuation, cap rates and property-level performance of national and local markets.

Survey authors said with few financing options and receding tenant demand, investors and real estate companies have shifted into a mode of managing and protecting their existing assets, with landlords cutting costs and rushing to sign or renew tenants -- in many cases offering sweet incentives and concessions such as free rent. The result is lower revenue and higher overall cap rates reported for the few investment sales that are being completed.

"Tenants are in the driver's seat, and landlords are in survival mode, trying to preserve revenue streams in one of the harshest ownership environments ever encountered," said Tim Conlon, partner and U.S. real estate sector leader for PricewaterhouseCoopers. "It will be survival of the fittest going forward, with owners who are able to remain financially strong being better positioned to capitalize on the buying opportunities that are to come."

Although sales have been weak, survey respondents expect buying opportunities to pick up in coming months as distressed assets from commercial loan defaults hit the market in larger numbers. Both private equity and institutional investors are preparing by disposing of certain assets, revving up potential joint partnerships, retiring debt and scrubbing their balance sheets, according to survey feedback.

However, a huge impediment is that, with the capital markets in disarray and few comparable transactions upon which to build a foundation, buyers and sellers can't agree on pricing.

In fact, one widely watched transaction-based index published at the MIT Center for Real Estate couldn't even produce a retail index for the fourth quarter due to the dearth of transactions. The overall sample size for various other property markets was "scarily low," acknowledged David Geltner, director of research at the MIT Center for Real Estate.

Of the data collected for other commercial property sectors, overall prices of property sold by major institutional investors fell by a record 10.6% in the fourth quarter of 2008 and 15% for the year, in line with similar analyses by CoStar Group, Inc. and other data providers.

The market uncertainty is perhaps best reflected in the confusion over cap rates. Most analysts agree there are just too few transactions to draw many conclusions.

Respondents to the Korpacz survey reported that overall cap rates have increased for most major markets and product types over the last during the quarter, a trend bolstered by an analysis of CoStar COMPs transaction data for office, industrial and multifamily sales over the last five quarters:

In fourth-quarter 2007, 180 closed transactions of Class A office sales of more than $5 million were recorded, trading at an average actual cap rate of 6.1% nationally. By the last three months of 2008, the average cap rate spiked to 7.6% on just 80 transactions, including a jump of more than 100 basis points between the third and fourth quarters. With sales results for the quarter still being collected, CoStar had recorded 42 closed transactions at an average actual cap rate of 7.9% as of March 18.

Investors closed 279 sales of Class A and B warehouse and distribution property in the fourth quarter of 2007 at an average cap rate of 7.1%. The number of transactions dropped sharply in fourth-quarter 2008, with the cap rate rising 100 bp. First-quarter 2009 is continuing to trend toward a sharp drop in transactions, with the cap rate edging up another 50 bp to a preliminary 8.6% as of March 18.

In the apartment sector, a look at sales totaling $5 million or more shows that 629 Class A properties exchanged hands in fourth-quarter 2007 at an average actual cap rate of 5.9%. For the same period a year later, 355 transactions sold and the average cap rate rose 90 basis point to 6.8%, thanks to a 50-bp jump between the third and fourth quarters. Though deal volume appears to be again dropping sharply in the first quarter, the cap rate for closed transactions was holding steady at 6.8% in the quarter to date -- the only major property category to hold the line on cap rate expansion.

Editor's Note: For news and updates on new development projects, land sales, significant deliveries and trends affecting development and construction, join the distribution list for CoStar's free weekly In The Pipeline column and newsletter. Check out this week's edition.
Another interesting result in the PricewaterhouseCoopers survey was the average amount of free rent offered by office landlords. Compared to a year ago, the average has increased sharply in several major metro office markets, including Boston, where average free rent increased from 2.15 to 6 months; Manhattan, where it grew from 4 ½ to six months; and in San Francisco, where it jumped from 3 ½ to six months. Warehouse landlords also have stepped up concessions significantly as tenants have melted away.

In the CBD office market, tenant concessions don't yet appear to be creating a lot of leasing activity, with many survey respondents reporting that deal flow is frozen.

"Tenants have the upper hand, but many of them are afraid to make critical near-term decisions because of the recession," noted one investor surveyed for the Korpacz report.

Subtle signs of weakness emerged in early 2008 as demand for suburban space waned, said an investor.

"By the latter part of 2008 tenants were no longer nine deep at the door and calls from prospective tenants began to dwindle."

A suburban office market respondent opined that "fundamentals will remain under pressure as demand weakens and more companies are forced to return space to the market," with the problems lingering for at least two more years.

Exhibit 2

The Comparative Sales Approach to Value

Laws, Regulations & Annotations

Property Tax Rules

TITLE 18, PUBLIC REVENUES CALIFORNIA CODE OF REGULATIONS
DIVISION 1. STATE BOARD OF EQUALIZATION

CHAPTER 1. STATE BOARD OF EQUALIZATION—PROPERTY TAX

Subchapter 1. Valuation Principles and Procedures (1–100)

RULE 4

Rule 4. THE COMPARATIVE SALES APPROACH TO VALUE.

Reference: Sections 110, 110.1, 110.5, 401, Revenue and Taxation Code. Article XIII A, Sections 1, 2, California Constitution.

When reliable market data are available with respect to a given real property, the preferred method of valuation is by reference to sales prices. In using sales prices of the appraisal subject or of comparable properties to value a property, the assessor shall:

(a) Convert a noncash sale price to its cash equivalent by estimating the value in cash of any tangible or intangible property other than cash which the seller accepted in full or partial payment for the subject property and adding it to the cash portion of the sale price and by deducting from the nominal sale price any amount which the seller paid in lieu of interest to a lender who supplied the grantee with part or all of the purchase money.

(b) When appraising an unencumbered-fee interest, (1) convert the sale price of a property encumbered with a debt to which the property remained subject to its unencumbered-fee price equivalent by adding to the sale price of the seller's equity the price for which it is estimated that such debt could have been sold under value-indicative conditions at the time the sale price was negotiated and (2) convert the sale price of a property encumbered with a lease to which the property remained subject to its unencumbered-fee price equivalent by deducting from the sale price of the seller's equity the amount by which it is estimated that the lease enhanced that price or adding to the price of the seller's equity the amount by which it is estimated that the lease depressed that price.

(c) Convert a sale to the valuation date of the subject property by adjusting it for any change in price level of this type of property that has occurred between the time the sale price was negotiated and the valuation date of the subject property.

(d) Make such allowances as he deems appropriate for differences between a comparable property at the time of sale and the subject property on the valuation date, in physical attributes of the properties, location of the properties, legally enforceable restrictions on the properties' use, and the income and amenities which the properties are expected to produce. When the appraisal subject is land and the comparable property is land of smaller dimensions, and it is assumed that the subject property would be divided into comparable smaller parcels by a purchaser, the assessor shall allow for the cost of subdivision, for the area required for streets and alleys, for selling expenses, for normal profit, and for interest charges during the period over which it is anticipated that the smaller properties will be marketed.

History: Adopted June 21, 1967, effective July 23, 1967.

Amended July 27, 1982, effective December 30, 1982.

Exhibit 3

Advanced Appraisal Handbook

(AH 502)

ESTIMATING ADJUSTMENT AMOUNTS

Several quantitative techniques can be used to estimate adjustment amounts. Recognized techniques discussed below include the following:[46]

- Paired sales analysis
- Statistical analysis
- Cost analysis
- Capitalization of rent difference (gain or loss)
- Discounting and time value of money concepts

PAIRED SALES ANALYSIS

Paired sales analysis is perhaps the most common method for estimating adjustments. The technique requires sales properties that are identical in all characteristics except the characteristic, or element of comparison, that is being measured. Alternatively, and less reliably, if the sold properties differ in more than one characteristic, adjustments must already have been made for characteristics other than the one being measured. The adjustment is estimated by simply subtracting one sale price from the other. In theory, paired sale analysis can be used to estimate the adjustment for any element of comparison, provided sufficient data are available.

Paired sales analysis is a popular technique for estimating the market conditions adjustment. Sales and resales of the same property or of highly similar properties are required. To make the adjustment, the appraiser should: (1) list the sales, (2) calculate the percentage change between the sale and resale prices, (3) divide this percentage change by the number of months between sales dates, and (4) apply this monthly estimate of the change in market conditions to comparable properties.

Paired sales analysis is also used for estimating adjustments for differences in physical characteristics. The paired sales must have occurred at the same time or have been adjusted for market conditions. To estimate an adjustment for physical characteristics, the appraiser first selects a sale property with a given set of characteristics. This sale property is then paired with another sale property (or properties) identical in all characteristics, except the one whose value is being estimated. The sale price of the first property is subtracted from the sale price of the second property in order to obtain an estimate of the value of the isolated characteristic.

In theory, paired sale analysis is a sound analytical technique. However, often there is an insufficient number of applicable paired sales—especially in the case of commercial properties. In addition, an estimated adjustment amount derived from only a single pair of sales may not be valid. However, when there are sufficient market data to apply the technique, paired sales analysis is practical and useful.

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[46] In addition to quantitative techniques of adjustment, some appraisal texts discuss qualitative techniques. Qualitative techniques compare comparable properties with the subject property by ranking them as "superior" or "inferior" (or similar terms) to the subject; adjustments not explicitly stated as either lump-sum dollar amounts or percentages. The subject property is then placed within the qualitatively ranked array of comparable sales in order to estimate its value. Appraisers often refer to this as "bracketing" the subject property. While this may be a widely used and valid appraisal technique, it is not in accord with provisions of Rule 4. Also, see footnote 34.

Statistical Analysis

Statistical techniques (e.g., linear and multiple regression) can be used in the measurement of adjustments. If an adequate database of sales data is available, multiple regression analysis is a valid technique for estimating the contributory value of selected elements of comparison that does not require the strict similarity between parcels required in most other methods of estimating adjustments. Using multiple regression analysis for this purpose involves the same methodology as valuation models based on multiple regression. A discussion of this technique is beyond the scope of this manual.[47]

Cost Analysis

An appraiser can use a cost analysis to estimate adjustment amounts, particularly for physical characteristics. Cost indicators such as an estimate of replacement or reproduction cost less estimated *depreciation*, an estimate of cost to cure, an estimate of deferred maintenance, etc., are used as the basis for adjustments in cost analysis. Although this method is widely used, its shortcoming is that the adjustment is not market derived—that is, estimated cost may or may not equal fair market value.

Capitalization of Rent Difference

Differences in rent (either a gain or loss) due to a specific property characteristic may be capitalized into an estimate of an adjustment amount. This technique is typically used to make adjustments for differences in physical characteristics, although it can be used for any difference between properties for which a permanent rent difference can be estimated. Obviously, an estimated capitalization rate is also required. For example, the subject property may have an elevator while a comparable property does not. Using market rental data, a rent differential for the two properties is estimated and capitalized—using direct capitalization—into an estimate of the adjustment. Both the rent difference and the capitalization rate should be market supported.

Discounting and Time Value of Money Concepts

An adjustment for above- or below-market leases (a property rights adjustment) can be estimated by discounting the difference between market and contract rent over the remaining term of the lease into a present value estimate. This technique requires an estimate of both the difference between market and contract rent and an appropriate discount rate. For example, assume that the sale price of a comparable property reflects a contract rent that is above market and that the lease has a remaining term of five years. A lump-sum adjustment is estimated by discounting the difference between contract and market rent at a market-derived discount rate over the five-year period.

An adjustment for non-market financing (a cash equivalent adjustment) can be estimated using discounting and time value of money concepts. Essentially, this technique involves discounting the periodic payment of the non-market loan into a cash equivalent, present value amount. The

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[47] See International Association of Assessing Officers, *Property Appraisal and Assessment Administration*, (Chicago: International Association of Assessing Officers, 1990), 159 and chapter 14.

payments are discounted at the market interest rate over either the remaining term of the loan or a shorter assumed holding period.[48]

ADJUSTMENT PROCESSES AND METHODS

As noted above, adjustments are made to the comparable sales prices to account for differences between the comparable properties and the subject property. The final result is a set of adjusted comparable sales prices representing estimates of what the comparable properties would have sold for had they possessed all of the important characteristics of the subject property. The adjusted sales prices thus become value indicators for the subject property. The process by which adjustments are made is sometimes referred to as "comparative analysis." This process involves several considerations, which include: (1) the direction and sign of adjustments; (2) the sequence of adjustments; (3) whether adjustments should be made in lump-sum dollar amounts or percentages; and, (4) whether adjustments should be made to the total property sale price or to a unit of comparison.

Direction and Sign of Adjustments

Adjustments to a comparable sale price are made toward, or relative to, the subject property. When a characteristic of a comparable property is inferior to that of the subject property, the adjustment to the comparable sale price is positive (i.e., the adjustment amount is added to the comparable sale price). When a characteristic of a comparable property is superior to that of the subject property, the adjustment to the comparable sale price is negative (i.e., the adjustment amount is deducted from the comparable sale price). This procedure applies to both lump-sum dollar adjustments and to percentage adjustments.

Adjustment to Total Sale Price or Unit of Comparison

Adjustments can be made to a total sale price, an appropriate unit of comparison, or both. Sometimes, adjustments are made to the total sale price for property rights conveyed, market conditions, cash equivalence, and non-real property items. This adjusted sale price is then converted into a unit of comparison (per square foot, per unit, per acre, etc.) that is further adjusted for the remaining elements of comparison (i.e., location, use, and physical and economic characteristics). Alternatively, all adjustments can be made to the entire property first, then this adjusted sale price can be divided by the relevant unit to derive a unit of comparison. The second method is more direct and preferable.

Lump Sum or Percentage Adjustments

Adjustments can be made as lump-sum dollar amounts or as percentage amounts. A general principle regarding adjustments is that they should be applied in the adjustment process based on the manner in which they were derived. Since most adjustments are derived in the form of dollar amounts (exceptions are the market conditions, i.e., time adjustment and perhaps the location adjustment), this leads to a general preference for dollar adjustments. Further, the particular

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[48] See Assessors' Handbook Section 503, *Cash Equivalent Analysis*.

sequence is not significant in the case of dollar adjustments, which is not always the case with percentage adjustments.

If multiple percentage adjustments are used, they can sometimes be applied in either an additive or multiplicative manner, producing different net adjustment amounts. "Additive" simply means that the percentages are added to arrive at a net percentage adjustment. "Multiplicative" means that the percentages are multiplied to arrive at a net percentage adjustment. A multiplicative adjustment implies that the factors considered in the adjustment process are causally related and hence correlated with each other. Multiplicative percentage adjustments should not be used unless this correlation can be verified, which is not often the case.

Sequence of Adjustments

A suggested sequence for adjustments is as follows: (1) property rights and interests conveyed; (2) cash equivalence; (3) non-real property items; (4) market conditions; (5) highest and best use and legally enforceable restrictions; and (6) location and physical and economic characteristics.

Adjustments for the first three items—property rights and interests, cash equivalence, and non-real property items—are made, typically, in terms of dollars. The result is an adjusted sale price that reflects property rights and financing terms equivalent to the subject property, and that reflects only real property. This provides an appropriate amount from which to apply the market conditions adjustment, since this adjustment is typically derived in a manner that does not reflect property rights and interests, cash equivalence, and non-real property items.

Next, the market conditions adjustment, typically a percentage adjustment, is made to the adjusted sale price described above. This provides an appropriate amount from which to apply the adjustments for highest and best use and for location and physical and economic characteristics.

Finally, adjustments for highest and best use and for location and physical and economic characteristics are made to the adjusted sale price that was further adjusted for market conditions as described above. If percentage adjustments are used, they should be applied as additives to this amount.

Presentation of Adjustments—Sales Adjustment Grids

The sales comparison approach uses a "column and row" (i.e., spreadsheet) format to organize the data for comparison and presentation. The sample sales adjustment grid on page 49 arrays the previously discussed elements of comparison in a standard sequence. The grid includes separate rows for each element of comparison and the adjustment relating to that element. Rows may be added as necessary in a given appraisal (e.g., several rows might be required to adjust for more than one physical characteristic). A row could also be added if the appraiser wishes to convert the adjusted sales prices to a unit of comparison (e.g., sale price per square foot, sale price per unit, etc.). The final two rows are designed to help the appraiser analyze the degree of comparability of each sale. They are used in the reconciliation of the adjusted sales prices into a single estimate of value. One row contains the absolute gross adjustment for each comparable sale. The other expresses the absolute gross adjustment as a percentage of sale price. The sample adjustment grid presented here is generalized. Particularly in the case of physical characteristics, attributes for

Exhibit 4

Mitchell

v.

County of Los Angeles

Mitchell v. County of Los Angeles (1997)
60 Cal. App. 4th 497 [70 Cal. Rptr. 2d 476]

[No. B111932. Second Dist., Div. Two. Dec 24, 1997.]

JOSEPH N. MITCHELL, as Trustee, etc., Plaintiff and Appellant, v. COUNTY OF LOS ANGELES, Defendant and Respondent.

(Opinion by Nott, J., with Fukuto, Acting P. J., and Zebrowski, J., concurring.)

COUNSEL

Duckor, Spradling & Metzger and Archie T. Wright III for Plaintiff and Appellant.

De Witt W. Clinton, County Counsel, and Derrick M. Au, Assistant County Counsel, for Defendant and Respondent.

OPINION

NOTT, J.-

Joseph N. Mitchell, as trustee for the Mitchell Family Trust, applied for a reduction in property taxes. The assessment appeals board (the AAB) denied the application. The superior court affirmed the AAB and entered judgment in favor of respondent County of Los Angeles (the County). We reverse the judgment for the reason the County failed to comply with the appropriate rules for an appraisal that involves an analysis based on comparable sales.

Factual Overview

The property involved in this matter is a single-family residence in Beverly Hills, consisting of an 8,287-square-foot home sitting on a 45,652-square-foot parcel of land. Improvements include a swimming pool and spa.

Appellant bought the property in November of 1985 for $2,550,000, and in the next year, made approximately $500,000 in improvements. Based on the sales price, the improvements, and the annual increases allowed by Proposition 13 (Cal. Const., art. XIII A, § 2), the property was appraised at $3,509,900 in 1993, which translates to an improved value of $424 per square foot. fn. 1

Appellant paid the taxes for 1993, and then filed an application for a reduced assessment. At the hearing before the AAB, appellant's expert [60 Cal. App. 4th 500] testified that the value of the property should be reduced to $3,025,000. The County presented evidence that the appraised value should remain where it is. The AAB agreed with the County. Appellant then brought an action for a refund. The trial court found that the County had presented admissible evidence to the AAB, and that there was substantial evidence to support the AAB's decision. The trial court thereafter entered judgment for the County.

Contentions on Appeal

Appellant contends that (1) the County's evidence of valuation was legally incompetent, and (2) there was no substantial evidence to support the AAB's findings.

Discussion

1. Standard of Review

[1] The primary issue on appeal involves a question of law, to wit, whether the assessor failed to comply with State Board of Equalization rules requiring adjustments to comparable sales data. We therefore review the matter de novo. (Main & Von Karman Associates v. County of Orange (1994) 23 Cal. App. 4th 337, 342 [28 Cal.Rptr.2d 432] (hereafter Main & Von Karman).)

2. The Evidence at the Hearing

[2] Under Revenue and Taxation Code section 167, in an administrative hearing involving an owner-occupied single-family dwelling, there is a rebuttable presumption that the owner's valuation is correct. In such an instance, the burden is on the County to overcome the presumption. fn. 2

At the subject hearing, the County provided evidence of three sales in the same locale within three months of the assessed valuation date (March 1, 1993) of appellant's property. The three sales were:

1. 940 Foothill Drive, which sold for $5,250,000. The residence was built in 1979 and measures 8,844 square feet on a 48,452-square-foot lot. The value of improvements was $594 per square foot. **[60 Cal. App. 4th 501]**

2. 513 North Doheny Drive, which sold for $5.5 million, was built in 1988. The lot size is 27,680 square feet. The house size is 11,571 square feet, with a value of improvements equal to $474 per square foot.

3. 812 North Foothill Drive, which sold for $3.3 million. The lot size is 29,490 square feet. The 6,858-square-foot residence was built in 1927. The improved value is $467 per square foot.

The problem that arose at the hearing was that M. Herrera, the assessor who did the actual appraisal, was not present at the hearing. Appellant complains that the absence of Herrera precluded effective cross-examination on the issue of whether adjustments had been made between each of the comparable sales as against appellant's property under rule 4(d). fn. 3 We note that on the work sheets prepared by Herrera, the improved value was determined by simply dividing the purchase price by the square footage of the residence.

An appraiser named Alan Whipp did testify. Whipp admitted that there was no specific mention on Herrera's work sheets that any adjustments were made. However, Whipp testified that it was common practice to either: (a) not adjust when the difference in value of a comparable sale to the subject property was so large that any adjustment would still exceed the appraised value of the subject property; or (b) to make the decision that no adjustment was warranted because the factors (size, age, location, amenities, etc.) canceled each other out. fn. 4 Whipp stated that even though no adjustments were mentioned, he felt that the appropriate items were considered by Herrera and were found to be zero.

Appellant's representative (Dave Middleton) moved to exclude any evidence of respondent's comparable sales on the basis of hearsay and because appellant was effectively precluded from cross-examining respondent on the subject of adjustments. Middleton's motion to exclude was denied. Middleton then questioned Whipp briefly as to some potential adjustments on the 940 Foothill property, and on the 513 North Doheny property. One of the **[60 Cal. App. 4th 502]** board members advised Middleton that all information should be given at this time, because there would be no other opportunity for him to present additional evidence at some future date.

Thereafter, appellant's expert, Craig Lipsey, testified. He had prepared five comparable sales, but the AAB requested that he give them just the three that were most favorable to appellant. Those three were:

1. 9425 Sunset Boulevard, which sold for $2 million. The 3,916-square-foot home was built in 1912 and sits on a 51,400-square-foot lot. The improved value is $511 per square foot.

2. 901 Rexford Drive, which sold for $3,150,000. The 8,116-square-foot house was built in 1988 and sits on a 40,500-square-foot lot. The improved value is $388 per square foot.

3. 620 Mountain Drive, which sold for $3,010,000. The 4,881-square-foot house was built in 1951 and sits on a 49,660-square-foot lot. The improved value is $617 per square foot. fn. 5

After making adjustments for location, age of the improvements, size of the respective homes, lot size, location, and amenities, Lipsey opined that the improved square foot value of the three comparable sales should be reduced to $339, $370, and $373, respectively. Lipsey was of the further opinion that the improved value of appellant's property should be $365 per square foot, which would result in a market value of $3,025,000.

Each side subsequently submitted proposed findings of fact and a proposed decision. Appellant once again requested that the AAB strike the evidence of comparable sales introduced by respondent under the authority of Main & Von Karman, supra, 23 Cal. App. 4th 337, a case which will be more fully discussed later. That request was evidently denied, as the AAB filed a three-page decision that had little resemblance to the suggested findings of fact submitted by the parties.

Instead, the AAB simply set forth the background information on the subject property; the comparable sales introduced by the County (with the notation that "No specific dollar or percentage adjustments were made"), the comparable sales introduced on behalf of appellant, and the conclusion of **[60 Cal. App. 4th 503]** the AAB that the 1993 fair market value of the subject property was $3,509,000. fn. 6

3. The Main & Von Karman Case

Main & Von Karman involved two parcels of commercial property. The taxpayer appealed the 1989 assessments, and presented evidence that, based on the income approach to value, the two parcels had been overassessed. The county assessor countered with the comparable sales method, and introduced raw data on the sales of several other properties. The taxpayer objected on the ground that the assessor failed to make adjustments to reflect the differences between the comparable sales and the subject properties as required by rule 4(d).

The assessor admitted that no adjustments were made. He offered a lack of county resources as one excuse. For the second, he contended that rule 4 was merely a guideline, which the assessor was not mandated to follow.

The appellate court rejected both arguments. First, the appellate court held that when the assessor relied on the comparable sales approach to value, it was mandatory that the assessor comply with rule 4 "to ensure statewide uniformity in appraisal practices (Xerox Corp. v. County of Orange (1977) 66 Cal. App. 3d 746, 753 [136 Cal.Rptr. 583]), and to assure that the property is assessed at its full value (Rev. & Tax. Code, § 401.5)." (Main & Von Karman, supra, 23 Cal. App. 4th 337, 343.) Next, the appellate court stated that the "lack of resources" argument was not "sufficient to relieve the assessor of his obligation to make adjustments to the raw data before presenting the comparable sales as evidence to the AAB." (Ibid.) The court concluded that "[t]he failure of the assessor to follow rule 4 requires reversal of the AAB's decision since the fair market value of the properties as determined by the AAB was based on evidence which was legally incompetent." (Id., at p. 344.)

4. Analysis of the Present Case

[3] In order to avoid the application of the holdings of Main & Von Karman, the County makes three arguments. First, the County contends that **[60 Cal. App. 4th 504]** its appraiser did in fact make an adjustment, and the adjustment was zero. We disagree. There was no competent evidence that Herrera did anything at all to consider adjusting the value of the comparable sales or the subject property upward or downward based on the interplay of the variety of factors that should have been considered, such as location, lot size, house size and age, and other amenities. Whipp had no firsthand knowledge of whether or not Herrera did in fact consider and make all appropriate adjustments, and in response to the leading questions asked him, said that even though not disclosed on the work sheets, Herrera "probably" made the adjustments. fn. 7 Just because there is an office policy to do so does not mean that it was in fact done. Further, even if Herrera did subjectively make the adjustments without disclosure on the work sheets, the County would fare no better. The shortcut practice of making an "overall adjustment" or a "range of values" estimation has been soundly rejected on the basis that the AAB must be provided with a solid evidentiary foundation for its decision. (Main & Von Karman, supra, 23 Cal. App. 4th at p. 343; Midstate Theatres, Inc. v. County of Stanislaus (1976) 55 Cal. App. 3d 864, 880-881 [128 Cal.Rptr. 54]; Dressler v. County of Alpine (1976) 64 Cal. App. 3d 557, 569, fn. 6 [134 Cal.Rptr. 554].)

Without citation to authority, the County next argues that the lack of adjustments is somehow justified in that the subject property here is residential whereas the properties in Main & Von Karman were commercial, "which are more complicated properties." That argument is without merit. Rule 4 does not distinguish between types of properties. Moreover, it is easy to imagine a situation where a commercial property (such as a freestanding **[60 Cal. App. 4th 505]** single-story 1,000-square-foot flower shop) would be far less complex to assess than a large residential property.

Finally, the County contends that even if the adjustments were not made, no miscarriage of justice occurred in this matter because the correct result was reached. The County asserts that in Main & Von Karman, the taxpayer pointed out several major differences between the comparable sales and the subject properties which could have had a major impact on valuation; whereas in the present case, appellant did not show what adjustments should be made to the comparable sales presented by the assessor. However, that argument ignores the central holding of Main & Von Karman, which was that the failure to abide by rule 4(d) made the assessor's evidence legally incompetent. We agree with that holding and reject the County's position.

5. Remand to the Trial Court and AAB

[4] Appellant claims that if we rule in his favor, the matter should be remanded to the AAB with directions to enter an assessment for $2.4 million. He reasons that such sum was his estimate of value going into the hearing, and if the County's evidence was legally inadmissible, then the County did not overcome the presumption that appellant's value was correct. Further, as the presumption of correctness was not overcome, the testimony of appellant's own appraiser (Lipsey) was superfluous, and thus the appropriate valuation should be $2.4 million. In support of his argument, he cites Prudential Ins. Co. v. City and County of San Francisco (1987) 191 Cal. App. 3d 1142 [236 Cal.Rptr. 869]. We disagree with appellant's claim.

Prudential does not support appellant's position. In that case, the matter was ordered back to the superior court for further remand to the AAB. The appellate court limited the new hearing before the AAB to a factual consideration under a cash-equivalent analysis. (191 Cal. App. 3d at pp. 1161-1162.) Therefore, the appellate court did not order that the taxpayer's value had to be accepted on remand. It simply prevented the assessor from proceeding with a pure de novo hearing in which the assessor might have attempted to present a new theory of valuation. (Id., at p. 1162, fn. 9.)

The same basic result occurred in Main & Von Karman, where the appellate court said: "[S]imply because 'substantial evidence of comparability was not produced at the county board hearing does not mean that none is available.' (Dressler v. County of Alpine, supra, 64 Cal. App. 3d at p. 571.) Remanding the matter to the AAB for further hearings, to be completed according to the standards prescribed by law, is the proper remedy." (23 Cal. App. 4th at p. 344.) **[60 Cal. App. 4th 506]**

Appellant argues that the County should not be given two bites of the apple to present evidence at a subsequent hearing that could have been presented at the first hearing. As attractive as that argument is, it seems to us that the overriding policy concern before us is that all property should be properly assessed and bear its fair share of property taxes.

In effect, appellant wishes us to accept a valuation of $2.4 million, which is over $600,000 less than his own appraiser said the subject property is worth. We see no fairness in a situation where a taxpayer's low-ball valuation would have to be mandatorily accepted because the assessor, for whatever valid or invalid reason, did not comply with rule 4(d). In this case, as in Dressler and in Main & Von Karman, a second hearing will occur. That hearing may or may not result favorably to appellant. However, appellant's inconvenience and expense may be ameliorated by the trial court's consideration of attorney fees and costs. (Rev. & Tax. Code, §§ 1611.6 and 5152; Gov. Code, § 800; Main & Von Karman, supra, 23 Cal. App. 4th at p. 344.)

Disposition

The judgment is reversed. The matter is remanded to the trial court. The trial court is ordered to issue a peremptory writ of mandate directing the AAB to hold a further hearing in a manner consistent with this opinion. Appellant is awarded costs on appeal. Appellant's request for attorney fees is transferred to the superior court.

Fukuto, Acting P. J., and Zebrowski, J., concurred.

A petition for a rehearing was denied January 16, 1998.

FN 1. The assessed valuation ($3,509,900) divided by the size of the residence (8,287 sq. ft.).

FN 2. Revenue and Taxation Code section 167 provides, in pertinent part: "(a) Notwithstanding any other provision of law to the contrary, ... there shall be a rebuttable presumption affecting the burden of proof in favor of the taxpayer or assessee who has supplied all information as required by law to the assessor in any administrative hearing involving the imposition of a tax on an owner-occupied single-family dwelling ...."

Property Tax Rule 321(b) of the California Code of Regulations, title 18, section 321, subdivision (b) also includes language similar to the above language.

FN 3. Rule 4 (Cal. Code Regs., tit. 18, § 4) is entitled "The Comparative Sales Approach to Value." It provides, in pertinent part: "When reliable market data are available with respect to a given real property, the preferred method of valuation is by reference to sales prices. In using sales prices of the appraisal subject or of comparable properties to value a property, the assessor shall: [¶] ... [¶] (d) Make such allowances as he deems appropriate for differences between a comparable property at the time of sale and the subject property on the valuation date, in physical attributes of the properties, location of the properties, legally enforceable restrictions on the properties' use, and the income and amenities which the properties are expected to produce."

FN 4. I.e., the age of a residence might be offset by the lot size of a comparable sale, etc.

FN 5. 620 Mountain Drive is next door to the property which is the subject of this appeal.

FN 6. In its response brief, the County states even though the AAB stated that "[n]o specific dollar or percentage adjustments were made," the trial court found that "an adjustment equal to zero was still an adjustment and that these were in fact made." While the trial court did make that statement during oral argument, no such finding was incorporated into the trial court's statement of decision and judgment. Instead, the trial court simply made the conclusionary rulings that the assessor's evidence was competent and admissible, and that the AAB's decision was supported by substantial evidence.

FN 7. The relevant questions (which were either compound or leading) between the assessor's representative (Harley Outten) and Whipp were reported as follows:

"Outten: Mr. Whipp, if you are nervous that the 1st comparable is a ... there's an age difference of 1979 built and a somewhat smaller lot. I know you didn't prepare this so I am going to ask you a question in general. Mr. Herrera prepared this. Do you know if he considered adjustments for any of these comparables including Foothill, Doheny, and the Foothill south of Sunset Boulevard? Did he make any adjustments that you know of and if not, did he consider any of those adjustments? Are you privy to that information?

"Whipp: We would have considered adjustments for differences in square footage and lot size, but none are actually written or indicated on the form.

"Outten: Is this normally the practice for the assessor's office to look at these things? Do they look over and say because of the large difference in value for that square footage that perhaps the adjustments were made. Now I know these are general adjustments, but do you think he considered the difference in say for instance lot size?

"Whipp: Yes.

"Outten: And he decided not to make adjustments for that. Do you think that was perhaps off-set by the age in some way?

"Whipp: Right.

"Outten: In other words, those adjustments although not made as a dollar or percentage form were probably considered and the adjustments he felt overall were 0.

"Whipp: Yes, I would say so."

Exhibit 5

Main & Von Karman Associates

v.

County of Los Angeles

Main & Von Karman Associates v. County of Orange (1994)
23 Cal. App. 4th 337 [28 Cal. Rptr. 2d 432]

[No. G013566. Fourth Dist., Div. Three. Mar 16, 1994.]

MAIN & VON KARMAN ASSOCIATES, Plaintiff and Appellant, v. COUNTY OF ORANGE, Defendant and Respondent.

(Superior Court of Orange County, No. 651662, Marvin G. Weeks, Judge.)

(Opinion by Sills, P. J., with Wallin and Moore, JJ., concurring.)

COUNSEL

Weil & Wright and Archie T. Wright III for Plaintiff and Appellant.

Terry C. Andrus, County Counsel, and Thomas C. Agin, Deputy County Counsel, for Defendant and Respondent.

OPINION

SILLS, P. J.

Plaintiff Main & Von Karman Associates (M&VK) appeals from a judgment denying its claim for refund of real property taxes. Because the county assessor failed to follow the mandatory provisions of rule 4 of the State Board of Equalization (Cal. Code Regs., tit. 18, § 4) in using the comparable sales approach to value in calculating the fair market value of the properties, we reverse.

Facts

M&VK is the owner of two commercial properties in Irvine that lie adjacent to one another. The "Main Street parcel" consists of a commercial building and land located at 2300 Main Street. It was purchased on December 31, 1985, for $9,625,000. The "Von Karman parcel" consists of an office building and land located at 17900 Von Karman Avenue. It was purchased the same day for $8,222,290. At the time of the sales, Western Digital Corporation was leasing both properties at a net rate of 95 cents per square foot. **[23 Cal. App. 4th 340]**

The county assessor assessed the parcels as of December 31, 1985, at an amount equal to their purchase price. As permitted by section 2 of article XIII A of the California Constitution (commonly known as Proposition 13), the assessor increased the assessments on each parcel by 2 percent per year. As of the March 1, 1989, lien date, the enrolled value of the Main Street parcel was $10,408,763, and the enrolled value of the Von Karman parcel was $8,728,465.

M&VK appealed the 1989 assessments, claiming that the Main Street parcel should have been assessed at $7.4 million and the Von Karman parcel should have been assessed at $5.6 million. An administrative hearing was held before Assessment Appeals Board No. 1 for the County of Orange (the AAB). Experts for M&VK, relying on the income approach to value, testified that there was a general oversupply of office space in the market, that a recent city zoning ordinance had severely limited the use of the properties, and that the buildings on the properties were now vacant. In addition, M&VK's experts stated that the prices for office space in the Irvine area had recently declined to 70 to 75 cents per square foot triple net as larger businesses emigrated to the southern part of the county. Applying guidelines established by state statutes for the income approach to value, M&VK's experts opined that the value of the properties on the 1989 lien date was $13 million.

The county assessor, on the other hand, used the comparable sales method to value the properties. He introduced into evidence sales of other land in Irvine by passing around a handwritten sheet showing the sale amount, zone, and location of these properties. He extrapolated from this data a market rate of 95 cents a square foot triple net for the Main Street parcel, and $1.20 a square foot triple net for the Von Karman parcel. On the basis of these rates, the assessor appraised the subject properties on the 1989 lien date at a little over $19 million.

M&VK objected to the use of these comparable sales on the ground that the assessor had failed to make adjustments to the sales data to reflect the differences between the subject properties and the comparable sales, as required by rule 4 of the State Board of Equalization, and on the ground that much of the information as to these sales was incorrect. M&VK's experts testified, for example, that on one sale the selling broker advised them that the property had never leased at 95 cents a square foot as stated by the assessor, and that on another sale, the selling broker advised them the lease was 75 cents a square foot, and not 95 cents a square foot as listed by the assessor. Other comparables involved either substantially newer construction (e.g., 1986, 1987), different markets (e.g., Mission Viejo), different types of **[23 Cal. App. 4th 341]** leases (e.g., full service gross), or were financing transactions that did not reflect the fair market value of the properties. In addition, M&VK pointed out that none of the assessor's comparable sales recognized concessions, such as free rent for the initial lease period, which would have to be made to attract new tenants.

The assessor admitted that no adjustments had been made, but offered two excuses. First, he explained that the State Board of Equalization rules were merely "guidelines" which the assessor was not required to follow, and his valuations fell within the general range of the comparable sales. He stated that, "what is happening in my comps is that I selected the comps in general area, in general time frame, in general use and age and size and quality rather than list a group of mathematical adjustments, I'm letting them unadjusted rank as superiors, inferiors, equals if you will, so that it can be seen by looking at them that our assessment falls well within the range of what they indicate," and that, "I haven't made adjustments on these comparables as a separate step, and I've explained that I am showing the range of the comparables for a reasonable amount to look at the description of the properties and the information. You see that they well support the assessed value which is below any indicators, and therefore did not feel that it was necessary to go step by step through a lot of elaborate mathematical adjustments."

Second, the assessor blamed the budgetary constraints placed on his office by Proposition 13. "Petitioner is objecting to ... a way that Assessor has done it for a long time, and really a way that has been established and is necessary because we really are not under the Prop 13 limitations in budget. We're not in a position to do a lot more sophisticated in large volume. We should be able to cost a lot more money to operate the Assessor's office. The sales of the area are extremely abundant. Whether or not they have the niceties of all being non-exchanges, or identical comps, or near in location, these all have similar uses. The age range is not that bad, the sizes are different, but the indicators that the Assessor's using is so much a square foot, so that adjusts to some degree for the size. We feel that there's ample comparable sales that show not a specific value, but a value above that which is on the assessment roll, which is all we feel we needed to show."

The AAB took the matter under submission. In its written findings of fact, the AAB dismissed much of M&VK's evidence as irrelevant, overruled its objection to the assessor's comparables, and rejected its evidence of value under the income approach to value. The AAB determined that the most reliable method of valuation is the comparable sales approach. Relying on the sales presented by the assessor, the AAB concluded that the fair market **[23 Cal. App. 4th 342]** value of the Main Street parcel was $116 per square foot, and the fair market value of the Von Karman parcel was $144 per square foot. These values were then reduced by "approximately 20 percent, to account for any reduction in value in the subject properties due to vacancy rates and/or lower rental rates, resulting from overbuilding in the area." Following this reduction, the AAB reassessed the Main Street parcel at $9.5 million, and the Von Karman parcel at $7.73 million. fn. 1

M&VK filed a petition for writ of mandate for refund of taxes paid. The superior court denied the petition, and M&VK appeals.

Discussion

[1a] M&VK contends that the county assessor failed to make the adjustments to the comparable sales data as required by rule 4 of the State Board of Equalization (Cal. Code Regs., tit. 18, § 4) before submitting the evidence to the AAB. [2] Because the contention goes to the methodology used (i.e., that the assessor violated the standards prescribed by law), the appeal presents a question of law. (Bret Harte Inn, Inc. v. City and County of San Francisco (1976) 16 Cal. 3d 14, 23 [127 Cal.Rptr. 154, 544 P.2d 1354]; County of Orange v. Orange County Assessment Appeals Bd. (1993) 13 Cal. App. 4th 524, 529 [16 Cal.Rptr.2d 695]; see also County of Stanislaus v. Assessment Appeals Bd. (1989) 213 Cal. App. 3d 1445, 1450 [262 Cal.Rptr. 439]; Prudential Ins. Co. v. City and County of San Francisco (1987) 191 Cal. App. 3d 1142, 1149 [236 Cal.Rptr. 869]; Jones v. County of Los Angeles (1981) 114 Cal. App. 3d 999, 1006 [170 Cal.Rptr. 879]; Dressler v. County of Alpine (1976) 64 Cal. App. 3d 557, 566 [134 Cal.Rptr. 554]; Midstate Theatres, Inc. v. County of Stanislaus (1976) 55 Cal. App. 3d 864, 880-881 [128 Cal.Rptr. 54]; cf. Union Pacific Railroad Co. v. State Bd. of Equalization (1991) 231 Cal. App. 3d 983, 992 [282 Cal.Rptr. 745].)

[1b] Rule 4 of the State Board of Equalization provides, in relevant part, that when the assessor uses the comparable sales method, the assessor shall correct noncash sale prices to their cash equivalent, and make other adjustments appropriate for such things as differences in physical attributes of the properties, differences in location, and the income which the properties are expected to produce. (Cal. Code Regs., tit. 18, § 4, subds. (a) &, (d).) fn. 2 The rule requires that each comparable sale be adjusted according to the Code of **[23 Cal. App. 4th 343]** Regulations to ensure statewide uniformity in appraisal practices (Xerox Corp. v. County of Orange (1977) 66 Cal. App. 3d 746, 753 [136 Cal.Rptr. 583]), and to assure that the property is assessed at its full value (Rev. & Tax. Code, § 401.5). County assessors have on occasion attempted to circumvent the rule by making "overall adjustments" to the comparable sales (see, e.g., Midstate Theatres, Inc. v. County of Stanislaus, supra, 55 Cal. App. 3d at pp. 880-881), or by using a "range of values" established by the market (see, e.g., Dressler v. County of Alpine, supra, 64 Cal. App. 3d at p. 569, fn. 6), but in each of these cases in which a shortcut method was used, the appellate courts held rule 4 was mandatory and must be strictly followed in order to provide the assessment appeals board with an evidentiary foundation for its assessment. (See, e.g., Prudential Ins. Co. v. City and County of San Francisco, supra, 191 Cal. App. 3d at p. 1149.) We see no reason to depart from this interpretation.

Here, the county assessor conceded he did not follow the requirements of rule 4. He mistakenly referred to them as "guidelines," and attempted to excuse the failure to comply with the rule by asserting that the assessor's office had never completed more detailed analyses of comparable sales, and that with the advent of the budgetary restrictions imposed by Proposition 13 the assessor's office was simply unable to comply with the rule. None of these excuses is sufficient to relieve the assessor of his obligation to make adjustments to the raw data before presenting the comparable sales as evidence to the AAB. The assessor's approach of merely giving the AAB the raw data and stating that the assessor's opinion was within the "range of values" shown by the data does not comport with the rule. As the Court of Appeal emphasized in a similar case, "The basic problem with the assessor's approach is that in practical terms it emasculates rule 4. Such an approach does not square with the spirit of rule 4 which carefully lists specific adjustments that are to be made, nor with the reasoning of the state board's general appraisal manual which states that, 'Each adjustment should receive separate and serious consideration' (Assessor's Handbook AH 501-102)." (Midstate Theatres, Inc. v. County of Stanislaus, supra, 55 Cal. App. 3d at p. 881.) **[23 Cal. App. 4th 344]**

Moreover, M&VK's experts pointed out glaring errors in the data on which the assessor was relying (e.g., actual rental rates of 75 cents per square foot as opposed to rates of 95 cents per square foot), which would have been corrected had the assessor done the work necessary to make the adjustments required by the rule. The experts also noted substantial differences between the comparable sales and the subject properties (e.g., age, size, location, zoning), which necessarily would have been factored into the assessor's opinion of value had he followed the rule. Permitting the assessor to submit information to the AAB that is patently incomplete would defeat the purposes of the rule: the assessment of the property at the proper full market value, and the securing of uniformity in assessments throughout the state. (Prudential Ins. Co. v. City and County of San Francisco, supra, 191 Cal. App. 3d at p. 1153.)

The failure of the assessor to follow rule 4 requires reversal of the AAB's decision since the fair market value of the properties as determined by the AAB was based on evidence which was legally incompetent. [3] However, we cannot, as M&VK asks, direct the AAB to accept M&VK's evidence or method of value. The comparable sales approach is the preferred method, and simply because "substantial evidence of comparability was not produced at the county board hearing does not mean that none is available." (Dressler v. County of Alpine, supra, 64 Cal. App. 3d at p. 571.) Remanding the matter to the AAB for further hearings, to be completed according to the standards prescribed by law, is the proper remedy.

Disposition

The judgment is reversed and the matter remanded to the trial court with directions to issue a peremptory writ of mandate commanding the AAB to conduct further hearings on M&VK's request for refund of property taxes. M&VK shall recover its costs on appeal. In addition, M&VK's request for an award of attorney fees (Gov. Code, § 800, Rev. & Tax. Code, §§ 538 & 5152) is transferred to the trial court for consideration in light of this opinion. (See Phillips Petroleum Co. v. County of Lake (1993) 15 Cal. App. 4th 180, 196-198 [18 Cal.Rptr.2d 765]; Prudential Ins. Co. v. City and County of San Francisco, supra, 191 Cal. App. 3d at pp. 1156-1161.)

Wallin, J., and Moore, J., concurred.

FN 1. There is actually a conflict in the AAB's assessment figures. At paragraph 14 of the written findings of fact, the Von Karman parcel is assessed at $7.33 million; however, in the "Decision" section it is assessed at $7.73 million.

FN 2. Rule 4 provides in pertinent part: "§ 4. The Comparative Sales Approach to Value. [¶] When reliable market data are available with respect to a given real property, the preferred method of valuation is by reference to sales prices. In using sales prices of the appraisal subject or of comparable properties to value a property, the assessor shall: [¶] (a) Convert a noncash sale price to its cash equivalent by estimating the value in cash of any tangible or intangible property other than cash which the seller accepted in full or partial payment for the subject property and adding it to the cash portion of the sale price and by deducting from the nominal sale price any amount which the seller paid in lieu of interest to a lender who supplied the grantee with part or all of the purchase money.... [¶] (d) Make such allowances as he deems appropriate for differences between a comparable property at the time of sale and the subject property on the valuation date, in physical attributes of the properties, location of the properties, legally enforceable restrictions on the properties' use, and the income and amenities which the properties are expected to produce...."

Exhibit 6

The Income Approach to Value

Laws, Regulations & Annotations

Property Tax Rules

TITLE 18, PUBLIC REVENUES CALIFORNIA CODE OF REGULATIONS
DIVISION 1. STATE BOARD OF EQUALIZATION

CHAPTER 1. STATE BOARD OF EQUALIZATION—PROPERTY TAX

Subchapter 1. Valuation Principles and Procedures (1–100)

RULE 8

Rule 8. THE INCOME APPROACH TO VALUE.

Reference: Sections 110, 401, Revenue and Taxation Code.

(a) The income approach to value is used in conjunction with other approaches when the property under appraisal is typically purchased in anticipation of a money income and either has an established income stream or can be attributed a real or hypothetical income stream by comparison with other properties. It is the preferred approach for the appraisal of land when reliable sales data for comparable properties are not available. It is the preferred approach for the appraisal of improved real properties and personal properties when reliable sales data are not available and the cost approaches are unreliable because the reproducible property has suffered considerable physical depreciation, functional obsolescence or economic obsolescence, is a substantial over- or underimprovement, is misplaced, or is subject to legal restrictions on income that are unrelated to cost.

(b) Using the income approach, an appraiser values an income property by computing the present worth of a future income stream. This present worth depends upon the size, shape, and duration of the estimated stream and upon the capitalization rate at which future income is discounted to its present worth. Ideally, the income stream is divided into annual segments and the present worth of the total income stream is the algebraic sum (negative items subtracted from positive items) of the present worths of the several segments. In practical application, the stream is usually either

(1) divided into longer segments, such as the estimated economic life of the improvements and all time thereafter or the estimated economic life of the improvements and the year in which the improvements are scrapped and the land is sold, or

(2) divided horizontally by projecting a perpetual income for land and an income for the economic life of the improvements, or

(3) projected as a level perpetual flow.

(c) The amount to be capitalized is the net return which a reasonably well informed owner and reasonably well informed buyers may anticipate on the valuation date that the taxable property existing on that date will yield under prudent management and subject to such legally enforceable restrictions as such persons may foresee as of that date. Net return, in this context, is the difference between gross return and gross outgo. Gross return means any money or money's worth which the property will yield over and above vacancy and collection losses, including ordinary income, return of capital, and the total proceeds from sales of all or part of the property. Gross outgo means any outlay of money or money's worth, including current expenses and capital expenditures (or annual allowances therefor) required to develop and maintain the estimated income. Gross outgo does not include amortization, depreciation, or depletion charges, debt retirement, interest on funds invested in the property, or rents and royalties payable by the assessee for use of the property. Property taxes, corporation net income taxes, and corporation franchise taxes measured by net income are also excluded from gross outgo.

(d) In valuing property encumbered by a lease, the net income to be capitalized is the amount the property would yield were it not so encumbered, whether this amount exceeds or falls short of the contract rent and whether the lessor or the lessee has agreed to pay the property tax.

(e) Recently derived income and recently negotiated rents or royalties (plus any taxes paid on the property by the lessee) of the subject property and comparable properties should be used in estimating the future income if, in the opinion of the appraiser, they are reasonably indicative of the income the property will produce in its highest and best use under prudent management. Income derived from rental of properties is preferred to income derived from their operation since income derived from operation is the more likely to be influenced by managerial skills and may arise in part from nontaxable property or other sources. When income from operating a property is used, sufficient income shall be excluded to provide a return on working capital and other nontaxable operating assets and to compensate unpaid or underpaid management.

(f) When the appraised value is to be used to arrive at an assessed value, the capitalization rate is to include a property tax component, where applicable, equal to the estimated future tax rate for the area times the assessment ratio.

(g) The capitalization rate may be developed by either of two means:

(1) By comparing the net incomes that could reasonably have been anticipated from recently sold comparable properties with their sales prices, adjusted, if necessary, to cash equivalents (the market-derived rate). This method of deriving a capitalization rate is preferred when the required sales prices and incomes are available. When the comparable properties have similar capital gains prospects, the derived rate already includes a capital gain (or loss) allowance and the income to be capitalized should not include such a gain (or loss) at the terminus of the income estimate.

(2) By deriving a weighted average of the capitalization rates for debt and for equity capital appropriate to the California money markets (the band-of-investment method) and adding increments for expenses that are excluded from outgo because they are based on the value that is being sought or the income that is being capitalized. The appraiser shall weight the rates for debt and equity capital by the respective amounts of such capital he deems most likely to be employed by prospective purchasers.

(h) Income may be capitalized by the use of gross income, gross rent, or gross production multipliers derived by comparing sales prices of closely comparable properties (adjusted, if necessary, to cash equivalents) with their gross incomes, gross rents, or gross production.

(i) The provisions of this rule are not applicable to lands defined as open-space lands by Chapter 1711, Statutes of 1967, nor are they applicable in all respects to possessory interests.

History: Adopted December 12, 1967, effective January 18, 1968.

Amended December 15, 1976, effective January 21, 1977.

Amended September 27, 1977, effective November 25, 1977.

Amended July 27, 1982, effective December 30, 1982.

Exhibit 7

SBE

Rule 2

ASSESSOR Los Angeles County	POLICY AND OPERATING PRACTICE MANUAL	NO. 5210-03-2
		EFFECTIVE 10-1-2012
		PAGE 1 OF 2
		DISTR. CODE 69
		FILE 5210-03-2.doc
ASSESSOR		PUBLISHED 9-27-2012

ACCEPTING SALE PRICE IN TRANSFER REAPPRAISAL (SBE RULE 2)

According to SBE Rule 2, and in conformance with the Revenue and Taxation Code Section 110, the words "full cash value" and "fair market value" mean the price at which a property would transfer for cash or its equivalent under prevailing market conditions and with the following provisions:

1) The property is exposed for sale in the open market for a reasonable time for the seller to find a purchaser and,

2) The buyer and seller have full knowledge of the uses to which the property may be put, both seek to maximize their gains and neither is in a position to take advantage of the exigencies of the other.

Effective September 25, 1991, the State Board of Equalization amended Rule 2 to provide that value means the price at which the "unencumbered or unrestricted fee simple interest in the real property (subject to any legally enforceable governmental restrictions) would transfer for cash or its equivalent..."

The State Board of Equalization also amended Rule 2 to reflect that when a reappraisable change in ownership occurs, the presumption that the sales price is the full cash value may be rebutted by evidence that the market value of the property is significantly more or less than the price paid for it. (A significant deviation is one of more than 5%.) The burden of proving value lies with the party seeking to overcome the presumption.

The presumption that the sales price is the full cash value does not apply to:

1) The transfer of any taxable possessory interest.

2) The transfer of real property when the consideration is in whole, or in part, in the form of ownership interests in a legal entity or the change in ownership occurs as a result of the acquisition of ownership interests in a legal entity.

3) The transfer of real property when the information prescribed in the change in ownership statement is not timely provided.

Rule 2 continues to provide that "if a single transaction results in a change in ownership of more than one parcel of real property, the purchase price shall be allocated among those parcels and other assets, if any, transferred based on the relative fair market value of each."

The amendment to Rule 2 is substantially in accord with our existing policy that the sale price be enrolled unless there is substantial and convincing evidence that the price is not an indication of market value. Departmental policy requires that appraisers provide written justification for not accepting the purchase price and references to supporting documentation. This information must be included in the comments section of the Paperless Transfer System (PTS).

The written justification should address the following questions:

1) Was this an arms-length, open-market transaction?
2) Was there favorable financing?
3) Was there any duress?
4) What was the listing price and how long was it on the market?
5) Is the contract rent at market? (if applicable)

The supporting documentation should include the following:

1) Aerial photographs of the subject and comparable properties.
2) Interior photographs of the subject and comparable properties, if available.
3) Property description and broker comments from MLS, Redfin, or other sources.
4) Subject lease information and market rent comparables. (if applicable)

The justification and documentation must be reviewed by the Supervising Appraiser prior to PTS approval.

George Renkei
Assistant Assessor

Property Tax Rules

TITLE 18, PUBLIC REVENUES CALIFORNIA CODE OF REGULATIONS

DIVISION 1. STATE BOARD OF EQUALIZATION

CHAPTER 1. STATE BOARD OF EQUALIZATION—PROPERTY TAX

Subchapter 1. Valuation Principles and Procedures (1–100)

RULE 2

RULE 2. THE VALUE CONCEPT.

Reference: Article 2, Chapter 3, Part 2, Division 1, Revenue and Taxation Code. Sections 110, 110.1, 401, Revenue and Taxation Code.

(a) In addition to the meaning ascribed to them in the Revenue and Taxation Code, the words "full value," "full cash value," "cash value," "actual value," and "fair market value" mean the price at which a property, if exposed for sale in the open market with a reasonable time for the seller to find a purchaser, would transfer for cash or its equivalent under prevailing market conditions between parties who have knowledge of the uses to which the property may be put, both seeking to maximize their gains and neither being in a position to take advantage of the exigencies of the other.

When applied to real property, the words "full value," "full cash value," "cash value," "actual value," and "fair market value" mean the prices at which the unencumbered or unrestricted fee simple interest in the real property (subject to any legally enforceable governmental restrictions) would transfer for cash or its equivalent under the conditions set forth in the preceding sentence.

(b) When valuing real property (as described in paragraph (a)) as the result of a change in ownership (as defined in Revenue and Taxation Code, Section 60, et seq.) for consideration, it shall be rebuttably presumed that the consideration valued in money, whether paid in money or otherwise, is the full cash value of the property. The presumption shall shift the burden of proving value by a preponderance of the evidence to the party seeking to overcome the presumption. The presumption may be rebutted by evidence that the full cash value of the property is significantly more or less than the total cash equivalent of the consideration paid for the property. A significant deviation means a deviation of more than 5% of the total consideration.

(c) The presumption provided in this section shall not apply to:

(1) The transfer of any taxable possessory interest.

(2) The transfer of real property when the consideration is in whole, or in part, in the form of ownership interests in a legal entity (e.g., shares of stock) or the change in ownership occurs as the result of the acquisition of ownership interests in a legal entity.

(3) The transfer of real property when the information prescribed in the change in ownership statement is not timely provided.

(d) If a single transaction results in a change in ownership of more than one parcel of real property, the purchase price shall be allocated among those parcels and other assets, if any, transferred based on the relative fair market value of each.

story: Adopted June 21, 1967, effective July 23, 1967.

Amended December 17, 1975, effective January 25, 1976.

Amended October 9, 1984, effective September 20, 1985.

Amended July 24, 1991, effective September 25, 1991.